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In the Supreme Court of the United States

OCTOBER TERM, 1993

INTEL CORPORATION, PETITIONER

v.

ULSI SYSTEM TECHNOLOGY, INC., RESPONDENT

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether an unlicensed infringer may escape liability for infringement of a patent on a product simply by having a licensee of the patent holder manufacture the infringer's product (using the infringer's design) and deliver the product to the infringer, who in turn sells the product.

RULE 29.1 STATEMENT

Petitioner Intel Corporation has no parent company and no subsidiaries other than wholly owned subsidiaries.

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OPINIONS BELOW

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JURISDICTION

The judgment of the court of appeals was entered on June 10, 1993. A petition for rehearing was denied on August 26, 1993. App., *infra*, 40a-42a. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

Section 271(a) of the Patent Act, 35 U.S.C. § 271(a), provides, in relevant part: "[W]hoever without authority makes, uses or sells any patented invention, within the United States during the term of the patent therefor, infringes the patent."

STATEMENT

This much-publicized patent case presents a broadly important and unsettled issue of law in the context of cutting-edge technology: whether an infringing product can be "laundered" by having it manufactured by a licensee of the patent holder.

The court of appeals misapplied the "first-sale" or "patent exhaustion" doctrine, which developed long ago to protect those who purchase patented articles from authorized sources. Under the first-sale doctrine, one who purchases an article that embodies a patent may use or resell that article at will without infringing the patent. *E.g.*, *Keeler* v. *Standard Folding Bed Co.*, 157 U.S. 659, 666 (1895).

In this case, by contrast, the patented invention was embodied in circuitry configurations that belonged to a third-party imitator, not the patentee or licensee. The licensee fabricated the imitator's products according to a design provided and owned by the imitator. The licensee did not own the products it fabricated. The Federal Circuit nonethe-

less held that the fabrication and physical transfer of a product that was never owned by the patentee or licensee was a "sale" by the licensee to the infringer that exhausted the *patentee's* rights, so that the infringing design was "laundered" or cleansed of patent infringement.

The importance of the Federal Circuit's decision is apparent. The panel dissent observed that "a wrong precedent in this particular context is a cause for concern, since it can only lead to even further confusion regarding an important issue of law." App., *infra*, 12a. The dissent from denial of rehearing en banc added, "the consequences * * * are economically far-reaching and likely to be harmful." *Id.* at 42a. Of particular concern were the effects on "American industry [within] a worldwide competitive environment," since under the Federal Circuit's rationale a U.S. patentee may be "held to have inadvertently lost the benefits of the patent system." *Id.* at 41a.

In this case there is as much judicial disagreement as is possible on a patent issue within the Federal Circuit's exclusive appellate jurisdiction (see 28 U.S.C. § 1292(c)(1)). There are directly conflicting district court decisions. Compare *Cyrix Corp.* v. *Intel Corp.*, 803 F. Supp. 1200 (E.D. Tex. 1992) (imitator may use foundry relationship with licensee to avoid liability for infringement), appeal pending, No. 93-1573 (Fed. Cir.), with App., *infra*, 24a-39a (district court ruling reversed by decision below: infringer cannot avoid liability by having its product made by licensee). See also *Timken* v. *Olin*, 41 F. 169, 171 (C.C.S.D. Ohio 1890) (rejecting "proposition that all that is necessary for an infringer to do * * * is to procure the manufacture of the infringing article by a licensee"). In addition, the Federal Circuit panel was divided, and there were three dissents from denial of rehearing en banc.

Parties on both sides of the issue have recognized its importance. Counsel for one of Intel's adversaries, for example,

wrote in a published article that "the substantial economic consequences of any decision by the Federal Circuit on this issue" lead him to "[a]ssum[e] a grant of certiorari," which would allow this Court – which has not addressed a "first-sale" issue since 1942 – "to reconsider the applicability of the rule of [*United States* v.] *Univis Lens* [*Co.*, 316 U.S. 241 (1942),] to products manufactured by a licensed foundry but owned and designed by that foundry's customers." Abramson, *When the Chickens Come Home to Roost: The Licensed Foundry Defense in Patent Cases*, COMPUTER LAW., Mar. 1993, at 1, 6.[1] And a ULSI spokesman admitted that the decision below had "ramifications * * * for the entire semiconductor industry." *Intel, Clone Maker ULSI at Odds Over Federal Court Decision*, PC WK., July 5, 1993, at 106. This case, in short, presents the kind of important issue that should not be left to a divided Federal Circuit alone, but should be reviewed by this Court.

A. Factual Background

An intensive program of research and development has made petitioner Intel the industry leader in semiconductor design and manufacturing. Intel introduced the first commercially available microprocessor in 1971. Intel integrated circuits (commonly known as "chips") have become the technology of choice within the computer industry. Intel's industry-leading inventions come at a high price – Intel spent more than one and one-half billion dollars on research and development from 1986 to 1990, and nearly as much in 1991 and 1992 alone. C.A. App. A406.

The product at issue in this case is a math coprocessor, which is an auxiliary computer chip that performs certain

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[1] Mr. Abramson represented the defendant in *Intel Corp.* v. *Chips & Technologies, Inc.*, No. C-92-20111 JW (EAI) (N.D. Cal.), one of the several cases that have arisen raising the exact issue presented in this case. That action was settled before any ruling by the trial court.

mathematical computations while the main microprocessor in a computer performs other functions. Intel owns the "Palmer patent" (U.S. Letters Patent 4,338,675 and U.S. Reissue Letters Patent 33,629), which describes a "numeric data processor" that was first incorporated into Intel's 8087 coprocessor in 1980 and more recently has been incorporated into Intel's 80387 coprocessor. The Palmer patent increases computation speed more than 100 times. C.A. App. A404.

1. *HP/Intel Cross-Licensing Agreement*

Within the computer industry, a multitude of competing innovators for years have engaged in research in related areas. Because intellectual property is the most valuable treasure in the business, each company patents as many innovations as it can. Improvements in the art frequently must build on previously patented inventions. Companies therefore either must design around existing patents that belong to their competitors, or risk infringing those patents, and meanwhile must expend sufficient resources to enforce their own patents against infringements by others.

The major participants in the industry in the 1970s and 1980s sought "patent peace." Rival innovators agreed to cross-license their existing and future patents for specified periods, so that each could develop its own products without worrying about the other's patented efforts in the same direction. Cross-licensing also increased the efficiency of their design efforts. Innovators did not need to design around as many patents and could redirect resources from patent litigation to research.

Hewlett-Packard (HP) and Intel are among the principal innovators in the industry. Their 1983 cross-licensing agreement is both simple and broad. Scarcely 300 words, the agreement recites that "HP and INTEL each want to increase their freedom of design by obtaining a license under present and future patents and patent applications owned or con-

trolled by the other" (C.A. App. A36), and provides, after an identical grant from HP to Intel, that

> INTEL hereby grants HP an irrevocable, retroactive, nonexclusive, world-wide, royalty-free license under all patents and patent applications owned and controlled by INTEL having a first effective filing date prior to January 1, 2000, said license to be effective until the expiration of said patents.

Id. at A37. The agreement does not empower either party to convey any rights to third parties. *Id.* at A36-A37.

2. *The Foundry Contract Between ULSI and HP*

HP sometimes acts as a contract manufacturer making other companies' parts according to designs that are developed and owned by the customers and then provided to HP. In industry parlance, it provides "foundry" services.

Respondent ULSI System Technology, Inc., like many other entrants into the computer industry, did not expend significant capital on manufacturing capacity *and* did not depend on innovative research to make its way. At the time of trial, ULSI's sole business was designing, having others fabricate, and selling the US83C87 coprocessor, an imitation of the Intel 80387 that, according to the only court that has addressed the question (App., *infra*, 28a-30a), infringes Intel's Palmer patent. Several other manufacturers, including Motorola, Weitek, and ITT, have designed math coprocessors that do not infringe the Palmer patent (C.A. App. A434). ULSI, however, did not design around the patent.

In 1991 ULSI recruited HP as a foundry for ULSI's 'C87 coprocessor. The ULSI/HP agreement made clear that HP would contribute only manufacturing capability and expertise, while ULSI would provide the design that could be used to transform raw silicon into a functioning coprocessor.

HP's role was to obtain blank silicon wafers and to etch ULSI's circuitry patterns on those wafers according to ULSI's design instructions. C.A. App. A38-A61, A412-A413. "ULSI supplied HP with the physical layout and design specifications for the 'C87 coprocessor, encoded on a magnetic design tape." App., *infra*, 3a n.3. But ULSI kept HP in the dark about the workings of the ULSI coprocessor: "HP did not receive complete functional diagrams or schematics." C.A. App. A412.

HP imprinted a pattern dictated by ULSI's design tape onto a series of quartz glass plates, also known as "reticles" or "masks." App., *infra*, 34a. This task was as menial as it sounds: any semiconductor foundry, whether or not licensed under Intel patents, could create identical reticles using ULSI's design tape. C.A. App. A412. Blank silicon wafers were exposed to light through reticles, forming a pattern that was chemically etched to become the circuitry of the coprocessor. *Ibid.* HP tested the wafers only to ensure that the fabrication was performed correctly; it did not test the functioning of the circuitry. *Id.* at A59-A60, A412-A413.

Although the ULSI/HP agreement was captioned a "sale" (C.A. App. A38), the agreement stated that HP was selling only "prototype and production fabrication of an integrated circuit designed by ULSI" (*ibid.*). ULSI at all times retained the ownership of the circuitry design (C.A. App. A43, A52); HP had no ownership rights whatever in the imprinted ULSI wafers, and had no right to use or sell those products (*id.* at A413).[2] HP could deliver the ULSI products only to ULSI, and had to return or destroy the design tapes and reticles upon completing the fabrication services. *Ibid.*

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[2] Similar agreements sometimes allow the foundry to sell the foundry customer's product to third parties under the foundry's label, but the foundry must pay a royalty *to the customer that supplied the design.*

When HP learned that ULSI's coprocessor was intended to be compatible with the Intel 80387, it asked ULSI whether ULSI "had any concerns about intellectual property rights." C.A. App. A411. ULSI replied that it had none. *Ibid.* ULSI did not tell HP that HP's cross-license with Intel was important to ULSI because ULSI intended to benefit from the license without paying for the privilege. Instead, ULSI *warranted* that it had not "improperly or unlawfully acquired the information and processes submitted to HP" to aid HP in fabricating the ULSI products (*id.* at A42, A51), *indemnified* HP from all liability for patent infringement that might arise from HP's fabrication of the ULSI products (*id.* at A42, A51), *licensed HP* "under any patent and mask works required to execute this Agreement" (*id.* at A44, A53), and, as the owner (as against HP) of the intellectual property rights in the design, *assumed* the "sole responsibility" to obtain patent or other protection for that property (*id.* at A43, A52).

B. Proceedings Below

In 1991 ULSI introduced its imitative coprocessor. When installed with ULSI's demonstration diskette, a computer would display the message, "The math coprocessor detected is an Intel 80387," even though a ULSI chip had been installed. C.A. App. A164. Intel determined that ULSI's coprocessor infringed the Palmer patent and filed suit in the United States District Court for the District of Oregon. *Id.* at A159-A168. ULSI stipulated to a permanent injunction against the misleading demonstration diskette. App., *infra*, 25a-26a. Intel did not sue HP because Intel has no quarrel with HP's performance of foundry services for ULSI. This dispute is between Intel, which owns the patent, and ULSI, which has infringed Intel's patent without paying *anyone* for the privilege.

After a hearing, the district court entered a preliminary injunction against ULSI's patent infringement. The district court held that the Palmer patent was valid and that ULSI's

coprocessor infringed. App., *infra*, 28a-32a. The court rejected ULSI's claim that, because HP was licensed to practice Intel's patent, ULSI was immune as well from liability for infringing the patent on the theory that HP had "sold" the ULSI-owned and -designed chips to ULSI. In the district court's view, ULSI in effect was claiming that HP had sublicensed ULSI to practice the Palmer patent; the court held that HP was not authorized and did not intend to grant ULSI a patent sublicense. *Id.* at 34a-36a. Moreover, the court added, "no *sale* took place" because "Hewlett-Packard never assumed any ownership rights in any ULSI product and had no right to use or sell any ULSI product." *Id.* at 36a-37a n.7.

A divided Federal Circuit panel reversed. App., *infra*, 1a-23a. The panel reached only the first-sale issue, but determined it with finality, holding that "ULSI is immune from infringement." *Id.* at 9a; see also *id.* at 10a ("we hold that the 'C87 coprocessors were insulated from Intel's claim of infringement because they were sold to ULSI by HP").[3]

The panel seized on the caption of the HP/ULSI agreement to determine that HP had managed to "sell" to ULSI the ULSI products that HP never owned. App., *infra*, 7a. Intel's right under the patent laws not to have a third party (as opposed to a licensee) practice its patents was irrelevant: "That ULSI, rather than HP, might have owned any existing intellectual property rights to the chips was a matter between ULSI and HP, and did not concern Intel." *Ibid.*

Judge Plager dissented, stating that the panel transformed "a sensible and socially desirable agreement between Intel and HP * * * into an unintended gift to all manner of infringers." App., *infra*, 22a. In his view, the "'patent exhaustion' or 'first sale' defense was simply lawyer argument by ULSI trying to

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[3] Judge Plager, in dissent, asserted (without contradiction from the majority) that the panel opinion "not only overturns the injunction but terminates the litigation." App., *infra*, 23a.

capitalize on the existence of an agreement between other parties (Intel and HP) in which ULSI had no part." *Ibid.*

Examining the ULSI/HP transaction in light of the policy of the patent laws, Judge Plager concluded that the "question of whose design and whose property was involved is not only relevant, but determinative." App., *infra*, 15a. The substance of the transaction was that HP "ma[de] [ULSI]'s invention for [ULSI]'s account." *Id.* at 18a-19a. Transfer of the fabricated product to ULSI did not constitute a "first sale" that exhausted Intel's patent because "HP never had ownership rights in the invention to sell to ULSI; if there was a 'sale,' it must have been of something else," namely HP's *services*. *Id.* at 21a. The first sale of the "*accused product*" was by ULSI to its customers (*id.* at 19a-20a) and did not take place under the patent or the HP/Intel license.

Judge Plager also noted that the testimony "indicate[d] unequivocally that neither party to the [HP/Intel] cross-license understood or intended their cross-license to bring [ULSI's] activity within the scope of the cross-license." App, *infra*, 19a. Therefore, because HP was not "authorized * * * to manufacture infringing embodiments of the Palmer patent at the behest of others," any "first sale" by HP to ULSI was not authorized and could not immunize ULSI from liability for infringement. *Id.* at 16a.

The court denied Intel's petition for rehearing and suggestion of rehearing en banc. App., *infra*, 40a. Judge Plager, joined by Judges Newman and Rader, dissented, noting that the panel opinion "frustrate[d] the contracting parties' reasonable commercial expectations, and destroy[ed] important property rights they had under the patent laws." *Id.* at 41a. They observed: "it is not the place of courts to limit or expand these arrangements * * * in a manner that is avowedly inconsistent with what the parties intended," particularly "when the consequences of doing so * * * are economically far-reaching and likely to be harmful." *Id.* at 41a-42a.

REASONS FOR GRANTING THE PETITION

In the course of enforcing a patent in favor of a leading innovator of the 19th century, this Court noted, "There are always those who are ready to gather where they have not sown." *Rubber Co.* v. *Goodyear*, 76 U.S. (9 Wall.) 788, 793 (1870). That observation holds just as true in the late 20th century. The Federal Circuit, however, misinterpreted patent law to prefer an unlicensed imitator over an innovator, and held that an infringer could escape liability merely by having its infringing product fabricated at the production facility of a patent licensee. As the dissenting judge noted, that is "both bad law and bad policy." App., *infra*, 22a.

The Federal Circuit gave its imprimatur to a method of patent evasion. The laundering technique that the court of appeals endorsed has appeared so far mainly within the multi-billion-dollar semiconductor industry, but – now bolstered by judicial approval – has limitless potential for application elsewhere, for it is not uncommon for one company to contract with another company to manufacture the first company's products. A patent infringer now "need only find a suitably cross-licensed company to be [its] manufacturing supplier" in order to disregard any licensed patent. Hustein & Greguras, *Cross-License Agreements Can Circumvent Patent Infringement*, S.F. DAILY J., Nov. 8, 1993, at 5.

The Federal Circuit made "[n]o effort * * * to justify this result on the grounds of public policy" (App., *infra*, 41a (en banc dissent)), nor did it purport to analyze the language, structure, or legislative history of the patent laws. Instead, the court reached its puzzling result under the perceived compulsion of a 1942 antitrust decision of this Court, *United States* v. *Univis Lens Co.*, 316 U.S. 241, and prior Federal Circuit decisions that addressed other issues. The older first-sale decisions involved sales of articles made by the patentee or by a licensee using an invention obtained from the patentee. They did not approve an attempt by an unlicensed party

to launder its own infringing invention by engaging a patent licensee to fabricate articles incorporating that invention.

I. THE ISSUE PRESENTED IN THIS CASE IS IMPORTANT TO AMERICAN INDUSTRY

This Court long ago recognized that the "vast pecuniary results involved in [patent exhaustion] cases, as well as the public interest," counseled particular judicial care in addressing the first-sale doctrine within different factual contexts. *Adams* v. *Burke*, 84 U.S. (17 Wall.) 453, 455 (1873). The basics of the first-sale doctrine have since become established, but this case presents a conspicuous new wrinkle, a wrinkle that presents the same "vast pecuniary results" and "public interest" that spurred this Court's previous attention to the issue.

The press immediately noted that the Federal Circuit's "ruling has broad implications for the semiconductor industry." Clark, *Intel Loses in Ruling on Patents*, S.F. CHRON., June 15, 1993, at C1. It is difficult to overstate the importance of that industry alone. Microchips virtually define the high-technology environment of the 1990s; not only personal computers, but a vast range of devices from automobiles to irrigation systems, now depend on semiconductors.

"[T]he ULSI case is not limited to semiconductors," however; "[c]ross-license agreements exist in innumerable variations relating to many technologies and industries." Hustein & Greguras, *Impact of the ULSI Case on High-Technology Industry*, S.F. DAILY J., Nov. 9, 1993, at 5. "Attorneys and executives concerned with intellectual property licensing and litigation will be fascinated by the * * * decision * * *. Its treatment of the doctrine of patent exhaustion has far reaching implications for a broad range of technologies * * *." Martin, Intel Corp. v. ULSI System Technology, Inc.: *Patent Exhaustion and Post-Sale Restrictions on the Use of a Component Made Under License*, 2 TEX. INTELL. PROP. L.J. 5, 6 (1993). Even if future cross-licenses might explicitly preclude the free-riding that occurred in this case,

the effect of exposing current licenses to that misuse should not be underestimated: the HP/Intel agreement, for example, covers all patents for which applications are submitted before January 1, 2000. Allowing a typical two years from the filing of an application to the issuance of the patent, the last patents under that agreement will not expire until 2018.

The decision in this case transforms any broad patent license to a *single* company into a vehicle for an unlimited number of infringers. Declaring open season on licensed, patented intellectual property can only hurt the competitive position of U.S. business in the world market. In addition, by penalizing innovation and rewarding imitation and deviousness, the Federal Circuit's decision thwarts the purpose of the patent laws.

A. The Patent Evasion Sanctioned by the Federal Circuit Is Likely to Become Widespread Because Cross-Licensing and Use of Contract Fabricators Are Common

The problem of the potential misuse of licenses by third parties is especially acute in industries in which cross-licenses are common. They have been very common in the computer industry, and helped spur the progress of that technology. See Merges & Nelson, *On the Complex Economics of Patent Scope*, 90 COLUM. L. REV. 839, 893-894 (1990). The cross-licensing parties licensed only innovators in related fields, not mere imitators who brought no intellectual property to the table. By inviting beggars to the banquet, the Federal Circuit has penalized the innovators in this leading segment of the American economy.

Cross-licenses also are common in other industries that depend on rapid technological innovation.[4] Because the Fed-

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[4] *E.g.*, *Agchem Producers Sow Plans for a Rich Harvest*, CHEMICAL WK., Aug. 18, 1993, at 33 (genetic engineering); *Siemens Agrees to Pay Medtronic $75 Million*, N.Y. TIMES, Sept. 12, 1992, at 35 (pacemakers); *Motorola, Philips OK Licensing Deal*, CHI. TRIB., Apr. 1, 1992, at C3 (telecommunications); *Westinghouse Electric Corp.*, WALL ST. J., Mar.

eral Circuit's decision opens cross-licenses in *all* industries to abuse by third-party imitators who make use of licensees' manufacturing facilities, strategies similar to ULSI's may be expected to appear in the fields of genetic engineering, telecommunications, and medical devices, among others.

Foundry and other contract manufacturing agreements also are widespread. Foundry arrangements are commonplace in the computer industry because manufacturing capacity for integrated circuits is overbuilt, and it is cost-effective for many companies to spend resources in improving designs rather than in adding their own redundant fabrication capability. Rappaport & Halevi, *The Computerless Computer Company*, HARV. BUS. REV., July-Aug. 1991, at 69, 72-75; *Small Semicon Firms Drop Fabs for Foundries*, ELECTRONIC NEWS, Mar. 7, 1988, at 16. Most of the principal market participants – including Intel – perform foundry services for smaller firms, and in turn have some of their own products manufactured by outside foundries. But the socially desirable situation in which one who is *entitled* to make a product contracts to have manufacturing performed by someone who can do it efficiently differs markedly from that in which an unlicensed imitator claims entitlement simply *because* it has chosen a foundry having a license with the patent holder.

The practitioners of the art of laundering infringing designs by using licensed foundries show no hesitation to publicize its advantages for those who would rather profit from others' research than do their own. Counsel for one company remarked that, by "making clear that these arrangements are OK, the decision [below] may well encourage others to

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24, 1992, at B4 (nuclear power); *Rapidly Made Models Won't Warp, Shrink*, ADVANCED MFG TECH., Dec. 15, 1990, at 4 (three-dimensional modeling); *Syntro: Focus on Animals Now*, INSIDE R & D, Oct. 3, 1990, at 4 (vaccines); Merges & Nelson, *supra*, 90 COLUM. L. REV. at 890 ("relatively automatic cross licensing" in automobile industry); *id.* at 891 (same in aircraft industry); *id.* at 900 (chemical industry).

adopt the ULSI approach." Clark, *supra*, S.F. CHRON. at C1 (quoting counsel for Chips & Technologies, Inc.). And counsel for ULSI declared that infringers no longer need worry about designing around patents or paying for licenses: "[A]ll we have to do is use a licensed foundry and we're all set." Orenstein, *Chip Makers Given New Defense Against Infringement Claims*, THE RECORDER (S.F.), June 15, 1993, at 1.

Intel's multi-billion-dollar research program is the target of the licensed-foundry device in this case, but Intel's position is not unique. If this Court allows the Federal Circuit's decision to stand, other innovators soon will find their intellectual property involuntarily shared with those who – like ULSI – give up nothing for the right to use that property.

B. The Federal Circuit's Decision Injures American Competitiveness in a Global Economy

In addition, the Federal Circuit's holding "potentially disadvantag[es] companies in a volatile [high-technology] industry * * * in competing world-wide." App., *infra*, 22a (panel dissent). In the 1990s and beyond, America's primary competitive asset in international markets – particularly in the high-technology sector – is intellectual property.

The Federal Circuit's decision dramatically weakens the protection of that key resource by easing the path for third parties to use licensed patents freely by engaging the licensee in a fabrication contract in which the licensee's patent rights play a legal but not a technological role. The court of appeals' decision will not go unnoticed overseas.

The decision also discourages "new and innovative arrangements for sharing emerging technology" within a "worldwide competitive environment," by increasing the risk that those arrangements will cost American companies their intellectual property. App., *infra*, 41a (en banc dissent). The Federal Circuit's decision discourages technology sharing

among American innovators facing foreign competition and exposes American companies to abuse by current and future contractual partners of their licensees. A foreign company could easily use a licensee – American or foreign – as a foundry in order to gain free access to a U.S. company's patents, at great cost to the American company's competitiveness here and abroad.[5] Indeed, cross-licenses, which are often necessary for U.S. companies to enter foreign markets effectively, already present some opportunities for abuse. See Spero, *Patent Protection or Piracy – A CEO Views Japan*, HARV. BUS. REV., Sept.-Oct. 1990, at 58, 64. The structure of continuing reciprocal relationships between large groups of companies within Japanese industry, for example, is especially conducive to misuse of cross-licenses to launder infringing products. Sakai, *The Feudal World of Japanese Manufacturing*, HARV. BUS. REV., Nov.-Dec. 1990, at 38, 48 (Japanese subcontractors regularly clone products licensed by American patentees to larger Japanese companies); see also Molina, *The US Revalues Its Electronics Patents*, NEW SCIENTIST, May 1, 1986, at 40, 43 (Japanese companies "participate in a complex mesh of cross-licensing").

Foreigners' intellectual property violations impose an annual cost of $40 to $60 billion on U.S. businesses. *Intellectual Property and International Issues: Hearings Before the Subcomm. on Intellectual Property and Judicial Admin. of the House Comm. on the Judiciary*, 102d Cong., 1st Sess. 8 (1991) (statement of Carla A. Hills, U.S. Trade Representative). Thus, there is a statutory U.S. negotiating objective to induce foreign governments to protect intellectual property adequately. See 19 U.S.C. § 2901(b)(10). The Federal Circuit's decision undercuts that objective. For example, the

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[5] Lost royalties also could have a significant impact on U.S. businesses, which in 1990 took in $12.6 billion more in patent license royalties from foreign companies than they paid out. Perez, *Exploitation and Enforcement of Intellectual Property Rights*, COMPUTER LAW., Aug. 1993, at 10, 12 (Fig. 2).

"Japanese patent system is short on disincentives to piracy and remedies for companies whose technologies are targeted." Spero, *supra*, HARV. BUS. REV. at 66. American negotiators will find it difficult to convince Japan that its system is inadequate when American patent protection is so fragile. It is still more difficult to argue in an arena such as the General Agreement on Tariffs and Trade that broader international intellectual property protections should be modeled on U.S. patent law, see Maskus, *Intellectual Property*, in COMPLETING THE URUGUAY ROUND 164, 170 (J. Schott ed., 1990), when the protections afforded by U.S. law can be evaded as easily as they were in this case. And, to undercut American negotiators' credibility further, the enforcement of Tariff Act Section 337 (19 U.S.C. § 1337) – already controversial – seems all the more trivial and arbitrary if a foreign infringer's ability to maneuver past the ITC depends on minor variations in the language of cross-licenses to which the infringer is not even a party. See App., *infra*, 9a-10a (distinguishing this case from *Intel Corp.* v. *ITC*, 946 F.2d 821 (Fed. Cir. 1991) (*Atmel*), because the license in that case was expressly restricted to the licensee's products).

The Federal Circuit's decision would exacerbate the trend to send manufacturing jobs overseas. Now, not only may a foreign manufacturing house exploit lower labor costs to draw contracts away from the United States, but manufacturers that are licensed to practice American patents can entice U.S. concerns with cut-rate access to the intellectual property of their American rivals.

C. The Federal Circuit's Decision Creates Perverse Incentives and Bestows Perverse Rewards That Thwart the Purpose of the Patent Laws

The purpose of the patent laws is to advance the progress of technology by ensuring that innovators have the exclusive right to the fruits of their inventions "as an incentive for their inventiveness and research efforts." *Diamond* v. *Chak-*

rabarty, 447 U.S. 303, 307 (1980). The Federal Circuit, by contrast, condoned the circumvention of valid patent rights by free-riders, thus encouraging imitation over innovation. Yet the court of appeals offered no *reason* to penalize innovators who contributed to the synergistic growth of an industry by allowing those who have added nothing to use those hard-won innovations for free. Rather than using patent law to encourage technological discovery, the Federal Circuit encouraged the discovery of others' patent licenses.

The decision distorts another incentive by encouraging arrangements based not on the most efficient use of manufacturing capacity, but on the opportunity to use patents without paying for them. Designers will pick foundries because of their patent license portfolios rather than their manufacturing skill. According to counsel for one designer: "[F]irms preparing to launch compatible products * * * recognized a way to turn their nascent foundry relationships to defensive advantage. Having heard about the patent cross-license agreements entered into by many large semiconductor companies in the 1970s, they formed foundry relationships with parties to these licenses." Abramson, *supra*, COMPUTER LAW. at 2-3.

The decision below also discourages innovation by companies that have entered into licensing agreements, including most major innovators in the U.S. computer industry. There is a drastically reduced incentive for a company like Intel to spend hundreds of millions of dollars in research each year if any imitative producer that has its infringing products fabricated by a licensee can use Intel's expensive inventions – and need not contribute to the research effort either by paying royalties or by cross-licensing patented technology.

The decision certainly discourages broad cross-licensing arrangements of the type that helped the American computer industry prosper. Although parties might contract around *this* decision, the court has made clear that free-riders may use patented inventions without paying, unless the particular

circumvention is expressly forbidden by the terms of the license. See Hustein & Greguras, *supra*, S.F. DAILY J., Nov. 9, 1993, at 5 ("transactions can be fashioned in clever ways to achieve what may amount to a legal circumvention of patent limitations"). Any firm that licenses its inventions consequently risks that some third-party imitator will appear with a new contractual arrangement that was not "expressly" prohibited, or a new argument for disregarding the patent based on the fabricator's cross-license rights, and will obtain a sympathetic ruling in the Federal Circuit.

D. This Court Alone Can Correct the Problem

No lower court is at liberty to disagree with the Federal Circuit on a patent issue. No circuit conflict is possible. The error in this case can be corrected only by this Court.

Perhaps for that reason, this Court rarely declines to review a substantive patent law issue on which one or more Federal Circuit judges have published an opinion dissenting from denial of rehearing en banc.[6] The three votes supporting rehearing en banc in this case demonstrate the importance of the issue presented and the need for review by this Court.

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[6] See *Morton International, Inc.* v. *Cardinal Chemical Co.*, 967 F.2d 1571 (Fed. Cir. 1992) (three judges dissenting from denial of rehearing en banc), rev'd, 113 S. Ct. 1967 (1993); *Eli Lilly & Co.* v. *Medtronic, Inc.*, 879 F.2d 849 (Fed. Cir. 1989) (one judge dissenting from denial of rehearing en banc), aff'd, 496 U.S. 661 (1990); cf. *Asgrow Seed Co.* v. *Winterboer*, 989 F.2d 478 (Fed. Cir. 1993) (one judge dissenting from denial of rehearing en banc), petition for cert. pending, No. 92-2038. But cf. *Malta* v. *Schulmerich Carillons, Inc.*, 959 F.2d 923 (Fed. Cir.) (one judge dissented from denial of rehearing en banc on retroactive application of circuit decision post-dating trial and standard for reviewing jury verdicts), cert. denied, 112 S. Ct. 2942 (1992).

II. THE FEDERAL CIRCUIT ERRONEOUSLY ENLARGED THE FIRST-SALE DOCTRINE

Long before there was a Federal Circuit, a federal judge put the issue in this case succinctly: "The mere statement of the proposition that all that is necessary for an infringer to do, in order to escape liability for his infringement, is to procure the manufacture of the infringing article by a licensee of the complainant, is sufficient for its refutation." *Timken* v. *Olin*, 41 F. 169, 171 (C.C.S.D. Ohio 1890). The proposition makes no more sense now than it did then, and the Federal Circuit's contrary holding should be overturned.

An analogy shows the unsoundness of the Federal Circuit's reasoning. A lawyer brings the manuscript of a brief to a printer's shop. The printer obtains blank paper, sets the submitted manuscript in type, and prints several copies of the brief. The lawyer then pays the printer a price per brief. The logic of the Federal Circuit compels the conclusion that the printer has "sold" the briefs to the lawyer, and in so doing has "sold" whatever intellectual property might inhere in the briefs, even though that intellectual property originated with the lawyer and was not changed by the printer. If the printer was licensed to print a third party's copyrighted material that the lawyer had plagiarized, the lawyer would be immune from an infringement action by that third party.

Substitute ULSI for the lawyer, HP for the print shop,[7] and patent for copyright,[8] and this case is on all fours. The relevant information – the *only* aspect of ULSI's product that infringed Intel's patent – was the circuitry that HP cut

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[7] "Foundries * * * are printing presses, and designers are writers." Barney & Waller, *Moore vs. Mead: Is Silicon Valley Obsolete?*, ELECTRONICS, Apr. 2, 1987, at 61 (paraphrasing Carver Mead, Cal Tech, co-inventor of design method that made semiconductor foundries possible).

[8] A virtually identical first-sale doctrine applies to copyrights. 17 U.S.C. § 109; *Bobbs-Merrill Co.* v. *Straus*, 210 U.S. 339 (1908).

into the reticles (*i.e.*, typeset) and etched into the blank silicon (*i.e.*, printed on blank paper), circuitry that follows exactly the pattern contained on the tapes (*i.e.*, manuscript) ULSI submitted to HP. HP no more "sold" infringing coprocessors to ULSI than Wilson-Epes Printing Company "sells" briefs to undersigned counsel. To use another analogy, it no more "sells" coprocessors than Fotomat "sells" photographs to the person who brings in the negatives. Yet the decision below depends entirely on the opposite premise.

The Federal Circuit stretched the first-sale doctrine out of shape to apply it in this case. The reasoning in *Univis Lens*, the antitrust case on which the court of appeals relied, makes that point clear.

A. The Federal Circuit Applied the "First-Sale" Doctrine to a Situation Not Addressed in Prior Cases and Not Covered by the Policy of That Rule

1. The venerable first-sale or patent exhaustion rule arose when patentees claimed that purchasers of the patented products (either from the patentee or a licensee) infringed the patent by their use of the purchased article. *E.g.*, *Adams* v. *Burke*, 84 U.S. (17 Wall.) 453 (1873). Before the current spate of litigation involving Intel, no court had ever suggested that the rule extended to exhaust a patentee's rights over infringing products that were designed by and manufactured exclusively for an unlicensed third party, but were fabricated by a patent licensee. When the issue arose contemporaneously with the origin of the rule, the court dismissed out of hand the argument that an infringer could evade liability so cheaply and easily. *Timken* v. *Olin*, *supra*.

The Federal Circuit provided no reason to extend the rule to such transactions, but apparently thought itself bound by a 1942 antitrust decision, *United States* v. *Univis Lens Co.*, *supra*. See App., *infra*, 6a, 9a-10a. *Univis Lens* condemned resale price restrictions imposed on purchasers of a product manufactured by the patentee's parent corporation

under a patent license. No unlicensed parties had any input into the intellectual property at issue in *Univis Lens*, and there was no infringement issue in the case. The Federal Circuit has endowed *Univis Lens* with more significance than the case can bear, and with significance that ignores controlling language in the older case. Because the most innovative American companies may suffer from an uncorrected misinterpretation of that 50-year-old antitrust case for at least another quarter century, the formalism of the Federal Circuit (equating any transfer of a patented device to an infringer, after fabrication by a licensee, with the patent-exhausting sale of a product incorporating a patented invention) should be rejected.[9]

The first-sale doctrine exists to protect *innocent* purchasers – who participate in neither design nor fabrication of a patented article – from suits brought by a patentee that has already received its recompense for the patent on the article

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[9] The Federal Circuit placed ULSI's activities under the rubric of cases that involved products made under the typical licenses to fabricate from the *patentee's* design – in other words, "private label" cases in which the patentee was upset because the licensee was doing exactly what it was licensed to do, but was allowing its customer to sell the product as if it were the customer's. See App., *infra*, 6a, 8a (citing *Unidisco, Inc.* v. *Schattner*, 824 F.2d 965 (Fed. Cir. 1987), cert. denied, 484 U.S. 1042 (1988), and *Lisle Corp.* v. *Edwards*, 777 F.2d 693 (Fed. Cir. 1985)). In *Lisle* the court of appeals rejected the contention that a licensee's customer infringed the patent because the licensee affixed the customer's label to the licensed product. In this case, however, the "customer" did not merely supply a label to be attached to the licensee's embodiment of the patented invention, but rather provided the specifications for the invention to be fabricated. In *Unidisco*, the court merely held that a distributor that purchased the licensee's patent-practicing product did not infringe the patent by reselling that licensed product. Neither *Lisle* nor *Unidisco* bears directly on the question whether an infringer may freely practice its infringing "invention" by hiring a licensee to fabricate it for the infringer's account *and according to infringing design specifications provided by the infringer and not by the licensee.*

sold. *E.g.*, *Keeler* v. *Standard Folding Bed Co.*, 157 U.S. 659 (1895); *Adams* v. *Burke*, *supra*. To carry out that purpose, the "first sale" that exhausts the patent holder's rights must be a sale by the party that owns (or has the right to use) the intellectual property incorporating the patented invention that inheres in the product sold.

2. This Court has never addressed the application of the first-sale doctrine to a situation in which the invention, or intellectual property, was divorced from manufacture. In all of this Court's first-sale cases, the seller had control over the design function as well as the fabrication and had *legally* obtained the rights to the patented invention.

Consideration of a mirror image of this case shows that it is the ownership of the design that incorporates the invention, not the manufacture of the physical article, that matters when the two *are* separate. If a licensee submitted a patented design to a third party to make for the licensee's benefit a patented product, the "first sale" would be from the licensee to the next purchaser – not *to* the licensee from the fabricator (who was entirely passive with respect to the intellectual property). The unlicensed fabricator would not infringe the patent by "selling" the licensee's product to the licensee. See *Southwire Co.* v. *ITC*, 629 F.2d 1332 (C.C.P.A. 1980).

In this case, ULSI at all times owned the intellectual property incorporating the patented invention that was inherent in ULSI's infringing chips. HP owned the blank silicon wafers, but once they were etched with ULSI's design HP possessed the wafers for the benefit of ULSI only. At no time did HP own the functioning coprocessor that was the infringing article. Yet the Federal Circuit declared that ownership of the design, *i.e.*, ownership of the patented "invention" that is embodied in the chip is *irrelevant* to the patent issue. App., *infra*, 7a. But that is exactly what the patent laws are intended to protect, and what the cross-licensees intended to share with each other.

The Federal Circuit "managed to take a shield the law provides to purchasers of products containing patented inventions and turn it into a sword to cut off the legitimate rights of the patent owner." App., *infra*, 11a (panel dissent). The court of appeals accomplished that result by blindly invoking the word "sale" to negate the protections of the patent, without considering just what the patent laws are supposed to reserve to patent owners – *i.e.*, the use of intellectual property incorporating the patented invention – and what, therefore, a patentee or its licensee would have to own and then relinquish in a sale in order to exhaust the patent.

B. There Was No "First Sale" Because HP Did Not Sell Intel's Invention to ULSI

Only a "*valid* sale and purchase" takes an article that practices a patent beyond the scope of the protections afforded the patentee. *Bloomer* v. *Millinger*, 68 U.S. (1 Wall.) 340, 351 (1864) (emphasis added). The question before this Court is whether there was a *valid* first sale when an unlicensed party (ULSI) illicitly practiced a patent by having an infringing product fabricated by a licensee (HP) that did not provide the infringing aspects of the product.

The question of what constitutes a "valid sale" that exhausts an inventor's right in its patent is a matter to be determined with reference to the policies of the patent laws, not merely as a matter of contractual interpretation. *United States* v. *Masonite Corp.*, 316 U.S. 265, 280 (1942); *General Talking Pictures Corp.* v. *Western Electric Co.*, 304 U.S. 175, 181, on reh'g, 305 U.S. 124 (1938).[10] When a trans-

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[10] The outcome of this case accordingly turns on "the inherent meaning and effect of the patent laws," *Keeler*, 157 U.S. at 666, not on the interpretation of contracts. As Judge Plager noted, "the duty that [ULSI] owes to [Intel] is determined by neither of [the HP/Intel and the ULSI/HP] agreements, but by the law of patent infringement." App., *infra*, 15a. The Federal Circuit's determinative holding was that a first sale under the patent laws occurs when a licensee fabricates a made-to-

action is examined for its effects on the operation of a patent, the substance, not the form, of the transaction controls the analysis. *Masonite*, 316 U.S. at 278.

In this case, however, the Federal Circuit ignored the substance of this common transaction and instead relied on the caption of the contract. Consideration of the *normal* foundry relationship clarifies who did what for whom in this case. The purchaser who orders the product and supplies the design is expected to own any necessary patent or the right to practice it; the ULSI/HP contract reflected precisely that understanding. C.A. App. A41-A44, A51-A53. There is no question whose product is being made, as the passive fabricator has no right to make, use, or sell the product on its own account; again, the ULSI/HP agreement is in accord.

In contrast to the panel majority, the district court *did* examine the substance of the transaction. It noted that HP provided "foundry *services* for the [ULSI] coprocessor," and "never assumed any ownership rights in any ULSI product and had no right to use or sell any ULSI product"; therefore HP could not and did not *sell* to ULSI anything that would release

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order product for an unlicensed third party who at all times owns the infringing "invention" underlying the product. The court of appeals did assert that additional contract terms might have changed the outcome if those terms forbade the licensee to do what HP did in this case. See App., *infra*, 10a (distinguishing *Atmel*, *supra*). But that holding simply establishes an illogical *presumption* that uncontemplated third parties may reap the benefits of a license unless the license's terms exclude that result. The Federal Circuit decision presents a *default* rule: any license that (like the HP/Intel agreement) does not *expressly* limit its benefits to the licensee will automatically be held to have given away all patent rights to uncontemplated third-party contractors for fabrication services. Because that interpretation supposedly is rooted in patent law, the court of appeals imposed it *despite* uncontradicted testimony that the parties to the license intended to do no such thing, and despite the utter failure of ULSI "to explain why the parties would have intended such a result." App., *infra*, 19a (panel dissent) (quoting *Atmel*, 946 F.2d at 827).

ULSI from liability for patent infringement. App., *infra*, 36a-37a n.7). Indeed, even one of Intel's adversaries has conceded in a published article that the question presented in these cases is "the applicability of the rule of *Univis Lens* to products manufactured by a licensed foundry but *owned* and designed by that foundry's customers." Abramson, *supra*, COMPUTER LAW. at 6 (emphasis added). In other words, one can find a sanitizing "first sale" in this case only by holding that a transfer *from* a *non*-owner (the foundry) *to* the owner (the customer) constitutes a "sale" – a bizarre use of language, to say the least. HP could not sell what it did not own. See *Mitchell* v. *Hawley*, 83 U.S. (16 Wall.) 544, 550 (1873).

Judge Plager, in dissent, reiterated that, "[b]ecause ULSI had provided its own integrated circuit design, HP never had ownership rights in the invention to sell to ULSI; if there was a 'sale,' it must have been of something else": blank silicon wafers and "*services*, measured per chip." App., *infra*, 21a. HP never contemplated that it was selling "to ULSI a chip containing the Palmer invention pursuant to the authority granted by the HP-Intel cross-license" (*ibid.*); therefore nothing that HP did sell to ULSI could have exhausted Intel's patent.

C. *Univis Lens* Does Not Support the Federal Circuit's Result

The Federal Circuit assumed that *Univis Lens*, a 50-year-old resale price maintenance case in which infringement had no part, somehow compelled the extension of the first-sale doctrine to this case. When carefully parsed, however, what this Court said about the first-sale doctrine in *Univis Lens* actually undercuts, rather than supports, the decision below.

1. The Court described the kind of sale necessary to "exhaust" a patent as "the vehicle for *transferring* to the buyer *ownership of the invention* with respect to that article." 316 U.S. at 252 (emphasis added). HP could not and did not transfer to ULSI "ownership of the invention" with respect

to the article at issue in this case – the ULSI imitation of the invention protected by the Palmer patent.

Both the reasoning and the express terms of *Univis Lens* condition patent exhaustion on a "*complete transfer of ownership*" of an article that is "*within the protection of the patent law.*" 316 U.S. at 249 (emphasis added). The basis for cutting off a patent holder's rights on sale of a patented article is that the patentee (either alone or in combination with a licensee) has received a reward "for the article *and* the invention which it embodies." *Id.* at 251 (emphasis added). Yet this case presents in clear form the separation of ownership of an invention from the provision of services that help realize that invention. It is quite clear that ULSI never paid HP (or Intel) for the "invention" that the ULSI coprocessors "embodied"; in fact, HP was never in a position to sell that invention because HP never owned it.

HP never owned "a product incorporating [Intel's] patented invention" (App., *infra*, 14a (panel dissent)) because ULSI owned the "chip designs, mask works, and physical layout computer data and processes" – that is, the physical embodiment of the circuitry invention that infringed Intel's patent (*id.* at 20a (quoting C.A. App. A43)). Whatever "transfer of ownership" from HP to ULSI might have been effected in the course of the foundry transaction, that transfer could not be "complete" because the intellectual property rights to ULSI's integrated circuit were never transferred; moreover, HP did not transfer to ULSI anything that was "within the protection of the patent law." HP never "retain[ed] the ownership of the patented article" (*Univis Lens*, 316 U.S. at 250), and therefore HP could not "relinquish[ ] * * * the patent monopoly with respect to the article sold" (*id.* at 249). Indeed, under the fabrication contract with HP, ULSI insulated its rights in its infringing design from HP (and thus from the patent license). ULSI cannot now claim the benefit of that license on the ground that HP sold ULSI what ULSI already owned.

Univis Lens also states that the first sale of any "article *manufactured under a patent*" puts that article beyond the control of the patent holder. 316 U.S. at 252 (emphasis added). In earlier cases, too, this Court recognized that the first-sale doctrine does not apply to an end product that as a whole embodies the invention of a patent, if the product was not manufactured or sold under the patent. *General Talking Pictures Corp.* v. *Western Electric Co.*, 305 U.S. 124, 125 (1938) (Brandeis, J.) (opinion on rehearing). The parties' mere characterization of a transaction as a "sale" does not dispose of the question whether the transaction exhausted all rights under the patent. See *id.* at 129 (Black, J., dissenting) (insisting unsuccessfully that any "sale" necessarily exhausted the patent). ULSI's chips were not "manufactured under a patent," because HP's paid performance of fabrication processes simply followed ULSI's infringing specifications and did not transfer to ULSI the "embodiment of the Intel patented invention," App., *infra*, 16a (panel dissent). The infringement arose from ULSI's specifications, not from the manner in which HP followed those specifications.

2. Furthermore, the facts of this case are radically different from those that led the Court in *Univis Lens* to apply the first-sale doctrine. In *Univis Lens*, lens blanks (embodying essential features of a *patented* finished lens) were fabricated according to the *patentee's* design by the licensee (the patentee's parent corporation) using a *patented* process, and then sold to third parties, whose only potential use of the blanks was in the completion of the *patented* finished lenses. 316 U.S. at 243, 246, 249. The open and authorized operation of the patent was clear at every step of every transaction in that case. In this case, by contrast, an *infringer*, ULSI, supplied a magnetic blueprint for infringement to HP; it did not acquire from HP the blueprint or the invention encoded in it and etched into the chips. ULSI alone made the first sale of a product that – illicitly – incorporated Intel's invention.

3. In any event, *Univis Lens* is of limited value in adjudicating a claim of infringement, particularly in this context. It makes little sense to assert that a 1942 case finding an antitrust violation controls a 1993 patent infringement issue that was not before the Court a half-century ago. The Court in *Univis Lens* was concerned with resale price maintenance conditions imposed on purchasers by licensees, and with the question whether patent rights might be exhausted by the sale of an article that could be used only to practice the patent. If an issue of this importance to American industry is to be governed by pronouncements of this Court, they should be pronouncements made in the context in which the issue now arises, not language wrested from a hoary antitrust precedent that indisputably did not present the same facts and policy issues as this case.

D. The Proper Application of the First-Sale Doctrine to Foundry Arrangements Is Plain

The proper application of first-sale principles to foundry arrangements is not difficult to discern in light of the purpose of the patent laws to protect patented intellectual property. In the absence of explicit contrary language in the license, whatever intellectual property the licensee-fabricator contributes to the product in the fabrication process should be immune from infringement suits. Any intellectual property the unlicensed designer contributes, however, should not be immune.

This result properly balances the protections granted the inventor by the patent with the expedition and efficiency sought by cross-licensing and foundry agreements. There is nothing efficient about allowing patent infringers to misuse foundry arrangements to avoid paying for protected intellectual property. Under the rule that we urge, those who pay have the benefit of protected intellectual property. Companies like ULSI that want something for nothing do not.

E. Because HP Did Not – and Could Not – Sublicense ULSI to Sell Intel's Invention, the First-Sale Issue Determines the Outcome of This Case

Because HP did not exhaust Intel's patent by fabricating ULSI's coprocessors, only a sublicense would protect ULSI from liability for infringement; ULSI's product was not licensed by Intel directly. A license, of course, entitles the *licensee* to produce, use, and sell the patented article *for its own benefit*, or to have another produce the article for the licensee's use or sale. When the article is produced according to the directions of, and for use or sale by, an unlicensed third party, that party must be licensed or sublicensed itself. *Carey* v. *United States*, 326 F.2d 975, 979-980 (Ct. Cl. 1964); see *E.I. du Pont de Nemours & Co.* v. *Shell Oil Co.*, 498 A.2d 1108, 1113-1114 (Del. 1985).

Incontestably there is no sublicense here. The Federal Circuit did not hold that Intel had licensed HP to sublicense third parties. As the district court held, "neither Intel nor Hewlett-Packard intended their agreement to be so broad as to grant the other party the power to sublicense any patent granted under the Intel/Hewlett-Packard agreement" (App., *infra*, 36a). The only appellate judge who reached the issue agreed that the HP/Intel cross-license could not be read silently to authorize sublicensing "[w]ithout something to explain why the parties would have intended such a result." *Id.* at 19a (emphasis omitted). See also 3 P. ROSENBERG, PATENT LAW FUNDAMENTALS § 16.01[1][b], at 16-13 (2d ed. 1993) (licensee may not sublicense "in the absence of an express provision in the license sanctioning sublicensing").

A contrary conclusion would be insupportable. The HP/Intel agreement does not expressly authorize sublicenses, and the ULSI/HP agreement restricts to the current owners all rights to use any intellectual property implicated in the manufacture of ULSI's coprocessors. HP and Intel agree that, between them, there was "no intent to immunize third

party infringers." *Id.* at 17a (panel dissent); see C.A. App. 408. And HP disclaimed any intent to sublicense ULSI to practice the Intel patent even if HP *had* that power. *Ibid.*

The Federal Circuit's holding on the first-sale issue excused ULSI's failure to obtain its own license. Once that erroneous application of the first-sale doctrine is corrected, ULSI cannot justify its infringement. The determination of the first-sale issue therefore controls the outcome of this case, and confirms ULSI's liability for infringement.

* * * * *

The Federal Circuit has considerable expertise in patent law, but its decision in this case rests *not* on that expertise, but on perceived marching orders from this Court. This Court, not a divided Federal Circuit, should have the last word on the subject.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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NOVEMBER 1993

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 92-1116.

INTEL CORPORATION,
Plaintiff-Appellee,

v.

ULSI SYSTEM TECHNOLOGY,
INC., Defendant-Appellant.

Decided: June 10, 1993.

John W. Keker, Keker & Brockett, San Francisco, CA, argued for plaintiff-appellee. With him on the brief were Jeffrey R. Chanin and Susan J. Harriman. Also on the brief were Paul M. Janicke, Sydney Leach, J. Paul Williamson and Wayne M. Harding, Arnold, White & Durkee, Houston, TX.

Michael A. Ladra, Wilson, Sonsini, Goodrich & Rosati, of Palo Alto, CA, argued for defendant-appellant. With him on the brief were Jere E. Webb and Charles F. Hinkle, Stoel Rives Boley Jones & Grey, of Portland, OR, of counsel.

Donald S. Chisum, Morrison & Foerster, of Seattle, WA, Michael A. Jacobs, Morrison & Foerster, of San Francisco, CA, and Bryan A. Schwartz, Morrison & Foerster, of Washington, D.C. were on the brief for amicus curiae, Chips and Technologies, Inc.

Before MICHEL, PLAGER, and LOURIE, Circuit Judges.

LOURIE, Circuit Judge.

ULSI System Technology, Inc. appeals from the order of the United States District Court for the District of Oregon granting Intel Corporation's motion for a preliminary injunction enjoining ULSI from infringing U.S. Patent Re. 33,629. *Intel Corp. v. ULSI Sys. Technology, Inc.*, 782 F. Supp. 1467, 21 USPQ2d 1922 (D. Or. 1991). Because the district court clearly erred in concluding that Intel had established a reasonable likelihood of success on the issue of infringement, we reverse.

BACKGROUND

Intel is the assignee of U.S. Patent Re. 33,629 to John F. Palmer, *et al.*, entitled "Numerical Data Processor."[1] The claims of the '629 patent are directed to the design and operation of a floating-point arithmetic processor capable of mixed precision calculations, mixed mode arithmetic calculations, and rounding operations. Intel has developed a line of math coprocessors[2] covered by the patent, including the Intel 8087, 80287, and 80387 coprocessors.

On January 10, 1983, Intel and the Hewlett-Packard Company (HP) entered into a cross-licensing agreement to "increase their freedom of design by obtaining a license under present and future patents and patent applications owned or controlled by the other." Under that agreement, Intel and HP each granted to the other an "irrevocable, retroactive,

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[1]The '629 patent is a reissue of U.S. Patent 4,338,675.

[2]A math coprocessor is a device which is designed to operate in conjunction with a microprocessor and is capable of performing mathematical computations at speeds up to 100 times faster than the microprocessor alone.

nonexclusive, world-wide, royalty-free license" under all patents and patent applications "having an effective filing date prior to January 1, 2000, said license to be effective until the expiration of said patents."

ULSI sells a math coprocessor known as the US83C87 ('C87 coprocessor) which is compatible with the Intel 80386 microprocessor and competes commercially with the Intel 80387 coprocessor. Since September 22, 1989, ULSI has purchased the 'C87 coprocessors from HP under an agreement entered into on August 2, 1988, in which HP agreed to manufacture the coprocessors for ULSI. As is apparently common in such "foundry" arrangements in the semiconductor industry, ULSI supplied HP with proprietary design specifications and HP then manufactured and shipped completed coprocessor chips to ULSI, which resold them as ULSI products.[3]

Intel first became aware of ULSI's 'C87 coprocessor sales on February 4, 1991. On July 29, 1991, Intel brought an action in the U.S. District Court for the District of Oregon alleging infringement of the '629 patent by ULSI's "making and selling, and inducing others to make, sell and use, the 'US83C87' [coprocessor]."[4] Intel filed a motion for a

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[3]Specifically, ULSI supplied HP with the physical layout and design specifications for the 'C87 coprocessor, encoded on a magnetic design tape. The design data were used by HP to imprint a design pattern onto a quartz glass plate. The imprinted plate known as a "reticle" or a lithographic mask was used in the chip fabrication process to etch the circuit layout of the coprocessor into blank silicon wafers. After the wafers were fabricated, HP conducted a visual inspection and a parametric test to detect any imperfections and errors that may have occurred during the fabrication process.

[4]Intel also brought an action against ULSI for alleged violations of section 32 and 43(a) of the Lanham Act, 15 U.S.C. §§ 1114 and 1125(a) (1988). The district court issued a stipulated order permanently enjoining ULSI from misleading consumers as to the origin of the 'C87 coprocessor.

preliminary injunction. In considering Intel's motion, the district court weighed several factors relating to injunctive relief, including the likelihood of Intel's success on the merits, irreparable harm, the balance of hardships, and the public interest.

The district court determined that the public interest favored neither party because the public's interest in the protection of patents was balanced by its interest in allowing an accused company to continue to operate until the issue of liability was fully adjudicated. Additionally, the court determined that the balance of hardships tipped in favor of ULSI because the 'C87 coprocessor was ULSI's only product and ULSI "would in all likelihood be forced out of business" if it were enjoined. However, the district court concluded that Intel had established a likelihood of success on the merits with respect to the issues of infringement, validity, and enforceability of the '629 patent. Furthermore, it determined that ULSI failed to rebut the presumption of irreparable harm that arose from Intel's "clear showing" of validity and infringement. Because the "likelihood of success on the merits and the irreparable harm (both of which favor Intel)" outweighed "the balance of hardships (which favors ULSI)," the district court granted Intel's motion.[5]

Intel Corp. v. ULSI Sys. Technology, Inc., Civil No. 9-742-JO (D. Or. August 12, 1991).

[5]ULSI filed a motion in this court for a stay pending appeal. Because we concluded that ULSI had shown that a substantial legal question existed on the issue of infringement, we granted the motion for a stay pending appeal. *Intel Corp. v. ULSI Sys. Technology, Inc.*, No. 92-1116 (Fed. Cir. January 14, 1992).

DISCUSSION

The issuance of a preliminary injunction under 35 U.S.C. § 283 (1988) is a matter of discretion for a district court. That discretion, however, is not absolute and must be reviewed in light of the equitable standards governing the issuance of injunctions. *Smith Int'l, Inc. v. Hughes Tool Co.*, 718 F.2d 1573, 1579, 219 USPQ 686, 691 (Fed. Cir.), *cert. denied*, 464 U.S. 996, 104 S. Ct. 493, 78 L. Ed. 2d 687 (1983). In determining whether a movant has established a right to preliminary injunctive relief, the district court must consider a number of factors, *viz.*, (1) whether the movant has sufficiently established a reasonable likelihood of success on the merits; (2) whether the movant would suffer irreparable harm if the injunction were not granted; (3) whether the balance of hardships tips in the movant's favor; and (4) the impact, if any, of the injunction on the public interest. *Hybritech Inc. v. Abbott Lab.*, 849 F.2d 1446, 1451, 7 USPQ2d 1191, 1195 (Fed. Cir. 1988). Each factor must be weighed and assessed against the others and against the form and magnitude of the relief requested. *Id.* We have cautioned, however, that a preliminary injunction is a drastic and extraordinary remedy that is not to be routinely granted. *Nutrition 21 v. United States*, 930 F.2d 867, 869, 18 USPQ2d 1347, 1349 (Fed. Cir. 1991); *Illinois Tool Works, Inc. v. Grip-Pak, Inc.*, 906 F.2d 679, 683, 15 USPQ2d 1307, 1310 (Fed. Cir. 1990).

In opposition to the motion, ULSI maintained that HP was permitted under the licensing agreement to act as a foundry for ULSI and that the sale of the coprocessors by HP to ULSI was a "first sale" that extinguished Intel's patent rights with respect to those products. The district court, however, rejected ULSI's argument because it determined that the licensing agreement did not grant HP the "power to sublicense" the '629 patent. On appeal, ULSI claims that the district court erred in concluding that the "patent exhaustion"

or "first sale" doctrine did not shield ULSI from Intel's claim of infringement.[6]

The law is well settled that an authorized sale of a patented product places that product beyond the reach of the patent. *See Bloomer v. Millinger*, 68 U.S. (1 Wall.) 340, 350-51, 17 L. Ed. 581 (1864). The patent owner's rights with respect to the product end with its sale, *United States v. Univis Lens Co.*, 316 U.S. 241, 252, 62 S. Ct. 1088, 1094, 86 L. Ed. 1408, 53 USPQ 404, 408 (1942), and a purchaser of such a product may use or resell the product free of the patent, *id.* at 250, 62 S. Ct. at 1093, 53 USPQ at 408. This longstanding principle applies similarly to a sale of a patented product manufactured by a licensee acting within the scope of its license. *See Unidisco, Inc. v. Schattner*, 824 F.2d 965, 968, 3 USPQ2d 1439, 1441 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1042, 108 S. Ct. 774, 98 L. Ed. 2d 860 (1988).

In the instant case, the issue as to whether ULSI is free from infringement liability turns on whether there was a sale of 'C87 coprocessors by HP to ULSI. Intel argues that the "patent exhaustion" doctrine does not apply because HP never sold a product to ULSI. Although Intel claims, as it must, that the 'C87 coprocessor infringes the '629 patent, it maintains that what was actually sold by HP under the foundry agreement was its fabrication *services* with an ancillary sale of wafers and chemicals. Intel asserts that HP could not have sold a *product* covered by the '629 patent because HP never had or retained any ownership rights in the 'C87 coprocessors. Thus, according to Intel, no sale ever

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[6]ULSI alternatively argues, as it did below, that the 'C87 coprocessor does not literally infringe the '629 patent. Because ULSI's defense based on the Intel-HP license is dispositive, we do not decide whether the district court erred in concluding that the claims of the '629 patent read on the 'C87 coprocessor. Additionally, ULSI does not contest the district court's conclusions regarding Intel's likelihood of success on the issues of invalidity and unenforceability, and we do not consider them.

took place that could support ULSI's "first sale" defense. That argument is incorrect.

Interpretation of a contract is a question of law which we review *de novo*. *See Interstate Gen. Gov't Contractors, Inc. v. Stone*, 980 F.2d 1433, 1434 (Fed. Cir. 1992). After reviewing the HP-ULSI contract, we cannot accept Intel's characterization of that agreement as one in which HP merely provided fabrication services to ULSI. That agreement, entitled "Terms and Conditions of Sale," is replete with references to the sale of semiconductor wafers (*i.e.*, chips) that incorporate the '*C87* coprocessor design. For example, the section of the agreement headed "Section 2: Production Fabrication" provided that HP "will sell CM0S34 wafers to" ULSI. That section recites prices for the chips and includes a delivery schedule for shipments of the chips to ULSI. Although the agreement also includes a section delineating the "engineering services" to be provided by HP, the agreement clearly involved the sale of chips, not merely the sale of fabrication services.

Nor, as Intel contends, must the licensed seller of a patented product own intellectual property rights to the product in order for there to be a sale. Intel makes much of the fact that the '*C87* chip was based on a design provided by ULSI. Intel confuses the issue of design origin with the issue of sale. Who designed the chip and whether it embodies inventions other than Intel's have no bearing on the controlling issue whether the '*C87* coprocessors were sold by HP to ULSI and thus extinguished Intel's patent rights relating to those products.

That ULSI, rather than HP, might have owned any existing intellectual property rights to the chips was a matter between ULSI and HP, and did not concern Intel. Intel does not dispute that HP was authorized under the broad terms of the licensing agreement to sell the chips at issue. To the extent that Intel had a patent covering the chips, HP's

conceded right to sell the chips deprives Intel of any claim of infringement, as long as HP sold the chips. If it had not granted that license or if the license had been limited in some relevant way, that would be a different case from the one before us. Intel might thereby have retained its right to proceed against those who entered into foundry agreements such as the present one. While Intel may not in retrospect be pleased with the deal that it made permitting HP to make unrestricted sales, it nevertheless granted HP that right in 1983, presumably for consideration it believed to be of value at that time. It cannot now renege on that grant to avoid its consequences.

We also reject Intel's contention that the sale of chips by HP to ULSI constituted a "*de facto* sublicense" prohibited by the licensing agreement. We found a similar argument to be "without merit and specious" in *Lisle Corp. v. Edwards*, 777 F.2d 693, 227 USPQ 894 (Fed. Cir. 1985). In *Lisle*, a licensed manufacturer sold products covered by the licensor's patent to a third party which resold them under its trademark. The licensor brought an infringement action against both the licensee and the third party on the basis that the manufacture of the patented product for the third party constituted a sublicense. Because such sublicensing was prohibited under the licensing agreement, the patent owner claimed that the products were infringing. The court in *Lisle*, however, concluded that the licensee's sales were authorized and that the resale by the third party did not create a sublicense. *Id.* at 695,227 USPQ at 895. Similarly, the sale by HP to ULSI here did not create a sublicense. HP did not empower ULSI to make Intel-patented chips or to use or sell any such chips except those lawfully sold to it by HP; these would have been the incidents of a sublicense.

Relatedly, we do not agree with the district court's conclusion that the sale of chips by HP to ULSI was not a "first sale" because HP was not authorized to sublicense ULSI to design products covered by the '629 patent. That

HP did not have the authority to sublicense the '629 patent to ULSI is irrelevant. The agreement between HP and ULSI was not a sublicense, but a contract for the manufacture and sale of chips. Thus, HP did not grant a sublicense; it sold a product, albeit one designed by its purchaser. ULSI is immune from infringement, not because it was a sublicensee, which it was not, but because HP was a licensed and therefore legitimate source of the chips. Moreover, ULSI was not required to be sublicensed in order to provide its chip design to HP.

Both parties cite our earlier decision in *Intel Corp. v. United States Int'l Trade Comm'n*, 946 F.2d 821, 20 USPQ2d 1161 (Fed. Cir. 1991) ("*Atmel*"), as supporting authority. *Atmel* is similar to, but distinguishable from, the instant case. Under the agreement in *Atmel*, Intel granted Sanyo a "non-exclusive, world-wide royalty-free license without the right to sublicense except to Subsidiaries, under Intel Patents which read on any *Sanyo* [devices] for the lives of such patents, to make, use and sell *such products*." (Emphases added). Intel alleged that Atmel, among others, violated 19 U.S.C. § 1337 (1988) by importing EPROMs (Erasable Programmable Read Only Memories) that infringed a number of Intel patents. Atmel claimed that its imported EPROMs were not infringing because they were manufactured and sold by Sanyo under its agreement with Intel. Intel, on the other hand, argued that Sanyo was not permitted to sell EPROMs to Atmel for resale as Atmel products because the licensing agreement only authorized Sanyo to sell *Sanyo* products.

As an initial matter, the court in *Atmel* expressly recognized the freedom from patent infringement of one purchasing products from a licensed party under a foundry agreement. The court stated that

> [i]f the Intel/Sanyo agreement permits Sanyo to act as a foundry for another company for products covered by the Intel patents, the purchaser of those licensed products

> from Sanyo would be free to use and/or resell the products. Such further use and sale is beyond the reach of the patent statutes. *See United States v. Univis Lens Co.*, 316 U.S. 241, 250-52, 62 S. Ct. 1088, 1093-94, 86 L. Ed. 1408, [53 USPQ 404, 408] (1942) (the first vending of any article manufactured under a patent puts the article beyond the reach of the patent).

Id., 946 F.2d at 826, 20 USPQ2d at 1166. Thus, the court agreed that Atmel would be shielded from Intel's claims of infringement if Atmel could establish that Sanyo was authorized to sell the EPROMs to Atmel.

In determining whether the licensing agreement provided for foundry rights, the court focused on what was meant by the "Sanyo limitation" in the agreement. The court concluded that the limitation precluded Sanyo from serving as a foundry for non-Sanyo EPROMs because Sanyo was only permitted to sell Sanyo products. Sanyo was prohibited from producing and selling EPROMs to Atmel for resale as Atmel products, and the court thus held that Atmel could not rely on the license defense. *Id.* at 828, 20 USPQ2d at 1167-68. In contrast, the licensing agreement between Intel and HP here contains no restriction on HP's right to sell or serve as a foundry.

In light of our discussion above, we hold that the 'C87 coprocessors were insulated from Intel's claim of infringement because they were sold to ULSI by HP, which was authorized to do so under its licensing agreement with Intel. Accordingly, we conclude that Intel cannot establish a likelihood of success on the issue of infringement.

To obtain reversal of a grant of a preliminary injunction, an alleged infringer must establish that a determination regarding one or more of the factors relied on by the district court was clearly erroneous. *New England Braiding Co. v. A.W. Chesterton Co.*, 970 F.2d 878, 882, 23 USPQ2d 1622, 1625 (Fed. Cir. 1992). Although none of the factors alone is

dispositive, the absence of a sufficient showing with regard to any one factor may, in light of the weight assigned to the other factors, preclude preliminary injunctive relief. *See Chrysler Motors Corp. v. Auto Body Panels of Ohio*, 908 F.2d 951, 953, 15 USPQ2d 1469, 1471 (Fed. Cir. 1990).

The district court's finding on the likelihood of success is clearly erroneous because it was based on a legal error concerning the application of the first sale doctrine. As to the other preliminary injunction factors, the district court presumed irreparable harm because it found that Intel had made a clear showing that the '629 patent was valid and infringed. Because that presumption was based on a clearly erroneous finding on the likelihood of success, it too was clearly erroneous. We discern no clear error in the district court's determination that the balance of hardships tipped in ULSI's favor and that the public interest favored neither party. In view of the totality of these factors, as weighed by the district court, we conclude that the district court abused its discretion in granting Intel's motion for a preliminary injunction.

CONCLUSION

The district court erred in determining that the Intel-HP licensing agreement did not provide ULSI with a defense against Intel's claim of infringement, a predicate to its finding a likelihood of success in proving infringement, and derivatively, irreparable harm, The district court's grant of Intel's motion for a preliminary injunction is therefore reversed.

REVERSED.

PLAGER, Circuit Judge, dissenting.

I respectfully dissent. ULSI has managed to take a shield the law provides to purchasers of products containing patented inventions and turn it into a sword to cut off the legitimate rights of the patent owner. While a wrong result in a

particular case is always unfortunate, a wrong precedent in this particular context is a cause for concern, since it can only lead to even further confusion regarding an important issue of law. In hopes that this case will not establish itself as such, I write to explain what went wrong.

In its simplest terms, the case is this. Company A and Company B are major competitors in a highly volatile industry. The industry experiences constant innovation in its products and processes, and is under great pressure from other domestic and foreign competitors. A and B both maintain large R & D operations, and obtain patents on their various innovations. Since both companies are engaged in continuing programs of research and development, they agree that it is in their mutual interest to avoid spending resources litigating with each other over patent rights rather than inventing.

In order to increase their freedom of design they cross-license each other in such a way that each is free to innovate and market their own similar products without fear of infringing upon the patent rights of the other. There is no intent to authorize third parties to make, have made, use, or sell the inventions covered by these patents beyond the rights the law accords to purchasers in the ordinary course in the marketplace.

Company C, a small company seeking to break in to the same market, approaches Company B with a proposition. C will provide B with details of its (C's) invention (a design similar to that patented by A). C will provide complete design and manufacturing specifications, and warrants to B in writing that C rightfully obtained the design involved and that it does not infringe the patent rights of others. Using its manufacturing facilities, B is to manufacture the item to C's specifications. B will provide the raw materials, and will be paid on a per completed unit basis. B, having excess manufacturing capacity, agrees, and produces the contracted-

for item. B then delivers the item to C, and C provides the finishing touches.

Later, C markets its product, describing it in terms that suggest it is the same as a product manufactured by A. A examines C's product, concludes that it is so much like A's product that it infringes one of A's patents, and sues C. C then defends on the grounds that, since B manufactured the item that infringes A's patent, and since B is immune from liability for infringement of A's patents under the A-B cross-license, C also is immune under the doctrine of 'first sale,' sometimes known as 'patent exhaustion.'

Of course C is wrong.

The principle of 'first sale,' simply stated, is that when a patent owner (or the owner's authorized licensee) sells to another a product which incorporates the patented invention, the other may convey the product to third parties free of any claim of patent infringement.[1] That is, third parties may use or sell the product without a license as such from the patent holder. This is but another variant on the common law rule that an owner of property may be estopped from claiming an interest in property which, through voluntary act of the owner, has found its way from the owner's transferee into the hands of a third party.[2]

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[1]See John W. Schlicher, *Patent Law: Legal and Economic Principles* § 8.05[1] (1992). We are not here concerned with the question of whether and to what extent a patent owner may impose conditions on the sale which bind future transferees. *See id.*

[2]In order to invoke the common law estoppel doctrine some courts required that the third party be a bona fide purchaser for value without notice. *See, e.g., Porter v. Wertz*, 68 A.D.2d 141, 416 N.Y.S.2d 254 (1st Dept. 1979), *aff'd* 53 N.Y.2d 696, 439 N.Y.S.2d 105, 421 N.E.2d 500 (1981) (suit for possession of a Maurice Utrillo painting entitled 'Chateau de Lion-sur-Mer'). U.C.C. § 2-403 extends the rule so that "any entrusting of possession of goods to a merchant who deals in goods

This rule has no application to the case of C for two reasons. First, the 'first sale' of the allegedly infringing product was by C to third parties, not by B to C. Second, the claimed activity of B must be within the scope of authority granted by the license from A in order for B's activity to immunize C; here it is not.

As for the first point, B did not make a sale to C of a product incorporating A's patented invention. It sold C the raw materials that went into the product. It manufactured C's product to C's specifications. It sold its manufacturing expertise, but the product was always C's, never B's (and assuredly not A's).

If B were to have manufactured a thousand extra embodiments of C's design, performed the finishing touches itself, and then sold them to third parties, would B's cross license with A protect it from a claim of conversion by C? The answer of course is "no." The issue of infringement under the cross-license – i.e., the rights of A and B vis-a-vis each other – is distinct from the question of C's legal rights against B or A, and vice versa.

If the issue is whether the chips made by B infringe A's patent, the fact that C rather than B designed them, or that C owns the manufactured item rather than B, would be irrelevant. If the accused product delivered to C infringes A's patent, then A has a cause of action for infringement of its patent right against both B and C.

B's defense is, I am not liable for infringement because I have a license from the patent owner.

C's defense is *not* the license; his defense is, I am not liable for infringement because I am a purchaser of the

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of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business." *See generally*, Sheldon F. Kurtz and Herbert Hovenkamp, *American Property Law* 152 (1987).

patented device in ordinary course in the marketplace. In which case the question is, did B sell the accused device to C, or did B sell C something else, like manufacturing services. The question of whose design and whose property was involved is not only relevant, but determinative.

As for the second point, the scope of B's authorization, neither A nor B intended by their cross-license to immunize third-party infringers of the patents of either. It is fundamental contract law that the A-B cross-license cannot afford rights and immunities to third parties that are not within the contemplation of the contracting parties. The duty that A and B owe to each other with regard to their own inventions and products is determined by the terms of the A-B cross-license; the duty that B and C owe to each other is determined by the B-C manufacturing agreement; the duty that C owes to A is determined by neither of these agreements, but by the law of patent infringement.[3]

In the case before us, A is Intel, B is Hewlett-Packard (HP), and C is ULSI. By law Intel has been granted the "right to exclude others from making, using, or selling" the invention claimed in the Palmer patent. 35 U.S.C. § 154 (1988). Intel alleges that ULSI "without authority . . . sells" a chip which is within the scope of the Palmer patent, and therefore is an infringer. 35 U.S.C. § 271(a) (1988). ULSI is correct that, if the C87 chip had previously entered the stream of commerce with Intel's permission via an authorized sale of the C87 chip by HP to ULSI, then ULSI's sales to others need not be authorized by Intel. *Bloomer v. Millinger*, 68 U.S. (1 Wall.) 340, 350-51, 17 L. Ed. 581 (1864). But

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[3]There is a possible exception – C might be considered a third party beneficiary of the A-B agreement (the cross-license). That would seem far fetched, given the nature of the business the parties are in, but it is possible. To arrive at that conclusion, however, would require finding the requisite conditions for third party beneficiary status for C. That is not achieved by a misinvocation of the patent exhaustion doctrine.

if ULSI's sale to others is the first sale of that chip (i.e. it is ULSI and not HP or Intel who launches the C87 chip into the stream of commerce), or if Intel never authorized HP to manufacture infringing embodiments of the Palmer patent at the behest of others, so that there could be no authorized sale by HP under the license, then ULSI's defense must fail. In my view, the defense fails on both counts.

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As an initial matter, if we assume for the sake of argument that HP sold an embodiment of the Intel patented invention to ULSI, we must determine whether that sale was authorized by the patent owner; absent authorization the transferee obtains no protection. *General Talking Pictures Corp. v. Western Elec. Co.*, 304 U.S. 175, 182, 58 S. Ct. 849, 853, 82 L. Ed. 1273 (1938); *Mallinckrodt, Inc. v. Medipart Inc.*, 976 F.2d 700, 703 (Fed. Cir. 1992). The answer to this question is found in the HP-Intel agreement.

The terms of the cross-license between Intel and HP are broadly stated. The cross-license notes that both parties are "engaged in continuing programs of research and development," and that both parties "want to increase their freedom of design by obtaining a license." In light of this expressed intent, HP and Intel then entered into a reciprocal grant – an "irrevocable, retroactive, nonexclusive, world-wide, royalty-free license under all patents and patent applications" filed before January 1, 2000, effective until the expiration of the designated patents.

It is correct that an appellate court approaches contract interpretation as a question of law. We thus owe no special deference to the trial court's view of that law; that is the meaning of review *de novo*. But that is not the same as saying we are free to ignore the trial court's factual determinations regarding the intent of the parties, based on testimony at trial. Especially is this the case when the matter

before us is not a final judgment but a preliminary injunction, a matter expressly within the broad discretion of a trial court.

Both parties to the agreement – Intel and HP – agree that the cross-license was intended only to provide each party with the freedom to conduct research and development work free of wasteful litigation, and that there was no intent to immunize third party infringers. For example, the Associate General Counsel and Director of Intellectual Property for HP testified that "[n]either Intel nor HP intended to grant the other the right to sublicense any patents licensed to the other under the patent cross-license agreement." Further, he testified that "HP did not intend to grant a sublicense under any Intel patents licensed to HP . . . ." *Jt. App.* at 408.

The trial court, after considering the evidence presented by the parties and following a hearing on the motion, agreed with Intel's interpretation of the contract. The trial court stated:

> In examining the breadth of the Intel/Hewlett-Packard agreement, it is clear that neither Intel nor Hewlett-Packard intended their agreement to be *so broad as to grant the other party the power to sublicense* any patent granted under the Intel/Hewlett-Packard agreement.

782 F.Supp. at 1474, 21 USPQ2d at 1928 (emphasis added).[4]

The use of the term "sublicense" by counsel and court must be understood to mean that the cross-license did not give HP power to authorize third parties to separately design and

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[4]Contrary to the majority's view, *Op.* at 1569, Intel did indeed dispute the authorization issue in its brief, under the subheading "The License Agreement Cannot Be Interpreted to Grant ULSI, an Unlicensed Infringer, a Sublicense to Launder its Product by Purchasing Foundry Services From HP." Intel argued that "the licensees never intended to provide third parties blanket immunity for their infringing activities, particularly where those third parties provided no consideration in return for such immunity." *Appellee brief* at 26.

manufacture (or have manufactured) products incorporating the patented invention. Thus HP could itself manufacture and sell products with the patented invention incorporated in them (and the purchasers of those products from HP would be protected in their use under the 'first sale' principle), but HP was not licensed to authorize others to do so.

In another context this court described as "without merit and specious" a patentee's argument to the effect that the activity involved was a prohibited sublicense. *Lisle Corp. v. Edwards*, 777 F.2d 693, 227 USPQ 894 (Fed. Cir. 1985). And on those facts, the argument was specious. In *Lisle* the patentee had granted the manufacturer (Lisle) a nonexclusive license to make, have made, use, and sell the patented tool. Lisle produced the tool in accordance with the patentee's design and paid the patentee a royalty on all sales. One of Lisle's customers, Snap-On Tools, purchased the patented tools but also arranged for Lisle to affix the tool with the Snap-On trademark. The patentee argued that the arrangement between Lisle and Snap-On was a "de facto sublicense," which made Snap-On a "de facto manufacturer." This court noted that "[t]he sales by Lisle were authorized by the nonexclusive license agreement. Resale did not create a sublicense." *Id.* at 695, 227 USPQ at 895.

Lisle does not stand for a general rule that an argument that sublicensing is prohibited under a particular license is necessarily "specious." The substance of the transaction at issue should control whether it is 'sublicensing,' and the terms of the license as intended by the parties should determine whether such 'sublicensing' is permitted. In *Lisle* the substance of the transaction was the licensee (Lisle) manufacturing a product containing the patented invention, with a subsequent authorized sale of the product to a third party (Snap-On) interested in buying it. Here, in contrast to *Lisle*, the third party, ULSI, purported to have no interest in buying the patentee's invention – the substance of the transaction was the licensee making the third party's invention

for the third party's account. And record testimony indicates unequivocally that neither party to the cross-license understood or intended their cross-license to bring this activity within the scope of the cross-license.

This is not the first time that the Federal Circuit has been called upon to determine the scope of a broad Intel license. In *Intel Corp. v. United States Int'l Trade Comm'n* 946 F.2d 821, 20 USPQ2d 1161 (Fed. Cir. 1991) (*Atmel*), Intel had similarly entered into broad cross-licenses with two foreign manufacturers (both with names including the word Sanyo). The two Sanyo companies entered into an agreement with a third company, Atmel, under which the Sanyo companies manufactured Atmel-designed chips which allegedly infringed Intel patents when offered for sale by Atmel in this country. This court held that the importation of such goods was in violation of the patent rights of Intel, since the Intel license to Sanyo did not permit the licensees to manufacture the designs of third parties and thus immunize the fruits of those designs from charges of infringement.

The court quoted with approval the ITC's description of the incongruity of the result argued for by Atmel:

> The interpretation of the licensing agreement as proposed by Atmel would mean that any company that was unable to obtain a license from Intel but still wanted to make its own parts practicing Intel patents could employ Sanyo as a foundry and circumvent Intel's patents. *Without something to explain why the parties would have intended such a result, the agreement will not be given this strained construction.*

Id. at 827, 20 USPQ2d at 1166-67 (emphasis in original).

2.

The second element to a successful 'first sale' defense is the existence of a sale of the *accused product* to the defendant – here ULSI – by the owner or someone authorized to sell

the product – here HP – prior to ULSI's own alleged infringing use or sale. The question is whether HP sold the accused product to ULSI. The preamble to the HP-ULSI agreement states: "[t]his Agreement details prototype and production fabrication of an integrated circuit *designed by ULSI* . . ." (emphasis added). *Jt.App.* at 38. The contract specifies that "the *ownership rights* to the chip designs, mask works, and physical layout computer data and processes shall be in the party who develops and designs the same." *Jt.App.* at 43 (emphasis added); those items were provided by ULSI. "[ULSI] will provide [HP] with the GDS-II data files containing the artwork database for the Part." ULSI "warrants that it *owns all the rights* to the information and processes including specifications, designs, instructions and Confidential Information provided to HP . . . [and] warrants that it has the full power and authority to supply and to disclose such information to HP." *Jt.App.* at 41 (emphasis added). ULSI further "warrants that it has not improperly or unlawfully acquired the information and processes submitted to HP for the purpose of this agreement." *Jt.App.* at 42. The contract then proceeds to indemnify HP against any liability for, *inter alia*, patent infringement.

The affidavit of Richard R. Duncombe, Sales Manager for the contracting HP fabrication facility, provides the background for these contractual provisions:

> I asked [the ULSI representative] whether he had any concerns about intellectual property rights. By this question, I wanted to make sure that ULSI's product could be fabricated without exposing HP to liability for patent, copyright, or trade secret infringement. [The ULSI representative] replied that ULSI had no concern about intellectual property implications. Nonetheless, in keeping with HP's custom and practice, ULSI agreed to indemnify HP against any claims of patent infringement, or other legal problems, which might arise from ULSI's design of the product.

Jt.App. at 411. Had HP intended to sell to ULSI a chip containing the Palmer invention pursuant to the authority granted by the HP-Intel cross-license, and had ULSI intended to use HP in such a capacity, none of the warranties and indemnifications would have been required.

Mr. Duncombe's affidavit further states:

> "HP has no ownership rights to ULSI's products, and no rights to sell or use ULSI's products. HP is required to return or destroy the magnetic design tape and reticles after HP completes the foundry services . . . ."

Jt.App. at 413. Because ULSI had provided its own integrated circuit design, HP never had ownership rights in the invention to sell to ULSI; if there was a 'sale,' it must have been of something else. Under the HP-ULSI contract, HP provided the blank silicon wafers upon which the ULSI design was etched. *Jt.App.* at 60. HP further provided the fabrication services for embedding the ULSI design on the blank HP wafer. *Jt.App.* at 57. ULSI paid HP for certain nonrecurring expenses, *Jt.App.* at 58, and paid a scheduled amount for each fabricated chip containing the ULSI design. *Jt.App.* at 60. Despite language which might imply that HP sold "chips," *Jt.App.* at 60, the overall context of the contract demonstrates that the sale was of *services*, measured per chip, rather than sale of any technology (be it Intel's or ULSI's), as embodied in each chip.

Thus HP basically sold its fabrication services and not the C87 chip with the allegedly infringing invention. The first sale of the C87 chip – the accused device in this infringement action, allegedly with the Palmer invention in it – was by ULSI and not by HP. That sale by ULSI was therefore within the scope of § 271, and is not a protected action of a purchaser in the marketplace.

Again, ULSI's argument confuses the question of whether HP manufactured a product that infringes Intel's patent rights

– allegedly it did, although that issue has yet to be definitively determined – with the question of whether that product was *owned and sold* by HP to ULSI, thus creating the 'first sale' defense.

3.

The district court understood that the parties to this suit and their arrangements fit the pattern described earlier. This is not a situation in which there is a dispute between the parties to a contract regarding their understanding of their respective contract rights. Rather, the district court recognized that the so-called 'patent exhaustion' or 'first sale' defense was simply lawyer argument by ULSI trying to capitalize on the existence of an agreement between other parties (Intel and HP) in which ULSI had no part. The district court rejected the defense, granted a temporary injunction against ULSI (a matter within her discretion), and prepared for trial on the merits.

The majority overrules this action by the district court, and effectively ends the case by granting judgment in ULSI's favor on this so-called defense. Thus a sensible and socially desirable agreement between Intel and HP is turned into an unintended gift to all manner of infringers. The result creates a disincentive among competitors to invent rather than litigate, potentially disadvantaging companies in a volatile industry such as this in competing world-wide. ULSI's position is both bad law and bad policy, and does not merit approval by this court.

Because the District Court did not abuse its discretion, commit an error of law, or seriously misjudge the evidence in holding that Intel was entitled to a preliminary injunction, I would vacate the stay and affirm the trial court's

judgment.[5] Even if I had reservations about the propriety of a preliminary injunction at this stage, which I do not, I believe the majority's conclusion that "ULSI is immune from infringement," *Op.* at 1570, is premature, since, if taken literally, it not only overturns the injunction but terminates the litigation.

[5]ULSI raises several issues of claim interpretation regarding which they believe the trial judge erred on her way to concluding that Intel showed the necessary likelihood of success on the merits. I have examined each of ULSI's arguments and find them unpersuasive. Since the majority disposes of the case on other grounds, these issues are not addressed in the majority opinion. See op. at n.6.

APPENDIX B

UNITED STATES DISTRICT COURT
D. OREGON

Civ. No. 91-742-JO.
INTEL CORPORATION, a Delaware corporation, Plaintiff,

v.

ULSI SYSTEM TECHNOLOGY, INC., a California corporation, Defendant.

Dec. 11, 1991.

John R. Bakkensen, Miller, Nash, Wiener, Hager & Carlsen, Portland, Or., for plaintiff.

Jere M. Webb, Charles F. Hinkle, Stoel Rives Boley Jones & Grey, Portland, Or., Michael A. Ladra, Joy A. Kruse, Wilson, Sonsini, Goodrich & Rosati, Palo Alto, Cal., for defendant.

OPINION

FRYE, District Judge:

The matter before the court is the motion of plaintiff, Intel Corporation (Intel), for a preliminary injunction (#4).

BACKGROUND

Intel is a manufacturer of math coprocessors, microprocessors, semiconductor memories, and microprocessor systems. Intel is the assignee of U.S. letters Patent 4,338,675 and U.S. Reissue letters Patent 33,629

(collectively, the "Palmer Patent") for an invention entitled "Numeric Data Processor." The Palmer Patent describes an architecture and method for performing floating point arithmetic operations in numeric data processor. The Palmer Patent is incorporated into an Intel product known as the 80387 math coprocessor (the "80387 coprocessor").[1] At issue in this litigation is the validity of the Palmer Patent and the alleged infringement of the Palmer Patent by defendant, ULSI System Technology, Inc. (ULSI).

ULSI manufactures a product known asthe US83C87 math coprocessor (the "US83C87 coprocessor"). Intel alleges that ULSI's US83C87 coprocessor incorporates key elements of the Palmer Patent. Intel contends that ULSI has infringed the Palmer Patent by making and selling, and inducing others to make and sell, the US83C87 coprocessor and similar math processors. Intel also contends that ULSI uses a demonstration diskette that falsely identifies the US83C87 coprocessor as an Intel product, thereby misleading consumers as to the origin and sponsorship of the US83C87 coprocessor.

On July 29, 1991, Intel filed this action against ULSI for patent infringement under United States patent law; for unfair competition and false designation of origin under the Lanham Trade-Mark Act; and for unfair competition under the laws of the State of Oregon. Intel seeks a preliminary injunction enjoining ULSI from (1) continuing to infringe or induce infringement of the Palmer Patent; (2) selling math coprocessors with demonstration diskettes that identify ULSI math coprocessors as Intel math coprocessors; and (3) continuing to make false representation of the origin and sponsorship of ULSI's math coprocessors. On August 12, 1991, the Honorable Malcolm M. Marsh, United States District Judge, signed a stipulated order permanently

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[1]A math coprocessor is an integrated circuit that allows computers to perform mathematical calculations at a high rate of speed.

enjoining ULSI "from selling or continuing to permit others to sell, any US83C87 math coprocessor with a diagnostic or demonstration diskette that identifies the ULSI math coprocessor as an Intel math coprocessor." Stipulated Permanent Injunction, p. 2, lns. 6-9. Thus, Intel now seeks only to enjoin ULSI's alleged infringement of the Palmer Patent.

CONTENTIONS OF THE PARTIES

Intel contends that it has met each of the elements necessary for the issuance of a preliminary injunction under 35 U.S.C. § 283: (1) that the Palmer Patent is valid and enforceable; (2) that ULSI's US83C87 coprocessor infringes the Palmer Patent; (3) that Intel is being irreparably harmed by ULSI's continued infringement of the Palmer Patent; and (4) that the balance of hardships and public interest weigh in favor of granting the injunction.

ULSI contends that Intel has failed to show a likelihood that it will succeed on the merits of its claims of validity and infringement. ULSI further contends that Intel cannot show either that it will be irreparably harmed or that the balance of hardships or public interest weighs in its favor.

APPLICABLE STANDARD

Under 35 U.S.C. § 283, a district court "may grant injunctions in accordance with the principles of equity to prevent the violation of any right secured by patent, on such terms as the court deems reasonable." In addressing a motion for a preliminary injunction under section 283, the court considers four factors: (1) the movant's likelihood of success on the merits; (2) the threat of irreparable harm to the movant should the motion be denied; (3) the balance of hardship between the parties; and (4) the impact an injunction will have on the public interest. *We Care, Inc. v. Ultra-Mark Int'l Corp.*, 930 F.2d 1567,1570 (Fed. Cir.1991). No one of these factors is necessarily dispositive. *Chrysler Motors*

Corp. v. Auto Body Panels, Inc., 908 F.2d 951, 953 (Fed. Cir. 1990). A court should consider and assess each of the four factors, balancing each against the others and against the magnitude of the relief requested. *Id.*

ANALYSIS

A. *Likelihood of Success on the Merits*

Under 35 U.S.C. § 282, a patent is presumed valid. "This presumption of validity places the burden of persuasion as well as the burden of going forward on the party asserting invalidity." *Chrysler Motors Corp.*, 908 F.2d at 953. At the preliminary injunction stage, however, this presumption does not apply. *Nutrition 21 v. United States*, 930 F.2d 867, 869 (Fed. Cir. 1991). Because of the extraordinary nature of injunctive relief, "the *patentee* carries the burden of showing likelihood of success on the merits with respect to the patent's validity, enforceability, and infringement." *Id.* (emphasis in original). This does not mean that a movant must prove beyond question its contentions of validity and infringement; rather, the patentee need only make a "clear showing" that its patent is valid and infringed. *Id.* at 869-70 (citing *Atlas Powder Co. v. Ireco Chems.*, 773 F.2d 1230, 1233 (Fed. Cir. 1985)).

In addressing the likelihood of success on the merits, ULSI contends that Intel has failed to demonstrate that it infringed the Palmer Patent. ULSI first argues that the US83C87 coprocessor does not infringe the Palmer Patent because it does not incorporate any of the five claims of the Palmer Patent. ULSI next argues that the Palmer Patent is invalid because all of the claims of the reissued patent are obvious in light of the prior art which Intel allegedly withheld from the Patent Office. Finally, ULSI makes two attacks on Intel's attempt to enforce the Palmer Patent. ULSI argues that inequitable conduct by Intel during the application for the Palmer Patent bars any attempt to enforce the patent. ULSI also argues that a cross-licensing agreement between Intel and

Hewlett-Packard provides ULSI with a defense against the infringement claim of Intel.

1. Infringement

Generally, a finding of infringement depends on whether the accused device falls within the scope of the asserted claims as properly interpreted. *Envirotech Corp. v. Al George, Inc.*, 730 F.2d 753, 758 (Fed. Cir. 1984). "Literal infringement requires that every limitation of the patent claim must be found in the accused device." *United States v. Telectronics, Inc.*, 857 F.2d 778, 784 (Fed. Cir. 1988), *cert. denied*, 490 U.S. 1046, 109 S. Ct. 1954, 104 L. Ed. 2d 423 (1989).

Intel contends that the US83C87 coprocessor literally infringes on every element of claims 5, 7 and 8 of the Palmer Patent. Intel's position is supported by the testimony of William Waite, a professor and chairman of the Department of Electrical and Computer Engineering at the University of Colorado. Waite examined the Technical Specification for the US83C87 coprocessor.[2] Affidavit of William Waite, para. 4. He also conducted his own tests on the US83C87 coprocessor. *Id.* Based on his examinations and tests, Waite found that the US83C87 coprocessor incorporates every element of claims 5, 7 and 8 of the Palmer Patent. *Id.* at paras. 5-8.

ULSI attacks Waite's analysis on a number of grounds. ULSI first contends that Waite never took into account the file history or any prior art in forming his claim interpretation. This contention is without merit, however. Waite read the file history and reviewed the prior art before reaching his conclusions. Rebuttal Declaration of Dr. William Waite, para. 8. ULSI next contends that Waite

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[2]Advanced Math CoProcessor Technical Specification. Affidavit of William Waite, Exhibit A.

failed to examine any of the detailed architecture of the US83C87 coprocessor. This contention is also without merit. Waite examined ULSI's detailed circuit schematics for the US83C87 coprocessor and found them "completely consistent" with ULSI's Technical Specification. *Id.* at paras. 3, 7. The record does not support ULSI's contention that Waite's analysis was inadequate or otherwise flawed.

Apart from its criticism of the analysis made by Waite, ULSI contends that it can establish that the US83C87 coprocessor does not infringe any of the five claims of the Palmer Patent. ULSI's position is supported by the testimony of Walstein Bennett Smith III, a Microprocessor Logic Design Engineer at Tredennick, Inc., a logic design and consulting firm based in San Jose, California. Affidavit of Walstein Bennett Smith III. Smith examined the Palmer Patent and compared it to the US83C87 coprocessor. *Id.* at para. 6. Following his analysis, Smith concluded that the US83C87 coprocessor does not infringe on the Palmer Patent because it does not contain the first and fourth elements of claim 5.[3]

The first element in claim 5 of U.S. Reissue Letters Patent 33,629 provides: "first means for converting said plurality of data formats to a file format having a fraction and exponent representation wherein said file format has a numeric fraction and exponent domain greater than any one of said plurality of data formats." Reissue Letters Patent 33,629, col. 27, lns. 8-12. The issue with respect to the first element of claim 5 revolves around whether reference to "plurality of data formats" in the claim imposes a limitation on the patent that would distinguish the US83C87 coprocessor from the invention claimed in the Palmer Patent. Taking "plurality of data formats" to mean "every single one of all

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[3]These two elements are also found in claims 7 and 8. Thus, the court's finding with respect to infringement of claim 5 will also be applicable to claims 7 and 8.

of the data formats," Smith concludes that this reference does impose a limitation which distinguishes the US83C87 coprocessor from the invention claimed in the Palmer Patent. *See* Affidavit of Walstein Bennett Smith III, p. 14, lns. 3, 10-11. Waite, taking "plurality of data formats" to mean at least two data formats, reaches the opposite conclusion. Rebuttal Declaration of Dr. William Waite, para. 22. After carefully reviewing both positions, the court agrees with Dr. Waite. Dr. Waite's interpretation of the term plurality is consistent with the ordinary, dictionary definition of the term.[4]

The fourth element in claim 5 of U.S. Reissue letters Patent 33,629 provides: "an arithmetic unit to perform arithmetic operations on said information in said file format, said arithmetic unit being coupled to said fraction bus." Reissue Letters Patent 33,629, col. 27, lns. 18-20. The dispute at issue in this element centers, in essence, on two phrases. First, the parties dispute whether the phrase "in said file format" refers (1) to the performance of "arithmetic operations" as Smith contends; or (2) to the "said information" as Waite contends. Next, the parties dispute the meaning of the term "file format" as it is used in element four. After reviewing the affidavits and analysis of both Waite and Smith, the court agrees with the interpretations of Waite. Waite's analysis is both credible and persuasive.

Based on these findings, Intel has shown that the US83C87 coprocessor infringes on every element of claims 5, 7 and 8. Accordingly, Intel has made a clear showing of infringement by ULSI.

2. Validity

ULSI contends that the Palmer Patent is invalid because all of the claims of the reissued patent are obvious in light of

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[4]Webster's Third New International Dictionary (1981) defines the term plural as relating to or consisting of or containing more than one. *Id.* at 1745. "Plurality" is the state of being plural. *Id.*

the prior art, which was not considered by the Patent Office. ULSI argues that several papers prepared by Jerome Coonen[5] in connection with the draft floating point standard of the Institute of Electrical and Electronics Engineers, Inc. when read in combination with the "UNRAU article"[6] demonstrate the obviousness of all five claims of the Palmer Patent. The position of ULSI is again supported by its expert, Smith. Affidavit of Walstein Bennett Smith III, paras. 21-25.

A patent may be proved invalid for obviousness under 35 U.S.C. § 103. When such a challenge is made, the court addresses "whether 'the prior art made obvious the invention as a whole for which patentability is claimed.'" *Symbol Technologies, Inc. v. Opticon, Inc.*, 935 F.2d 1569, 1576 (Fed. Cir. 1991) (quoting *Hartness Int'l Inc. v. Simplimatic Eng'g Co.*, 819 F.2d 1100, 1108 (Fed. Cir. 1987)). Rather than picking and choosing among the individual elements of prior art references to recreate the claimed invention, the court "look[s] for 'some teaching or suggestion in the references to support their use in the particular claimed combination.'" *Id.* (quoting *Smithkline Diagnostics, Inc. v. Helena Lab. Corp.*, 859 F.2d 878, 887 (Fed. Cir. 1988)).

Under the test set out in *Graham v. John Deere Co.*, 383 U.S. 1, 86 S. Ct. 684, 15 L. Ed. 2d 545 (1966), the court examines four different factors in making its determination:

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[5]H. Stone, et al., Draft on a Floating-Point Standard from Discussions with H. Stone, W. Kahan, and J. Coonen (April 24, 1978) (Declaration of Joy A. Kruse, Exhibit 7); J. Coonen, Specifications for a Proposed Standard for Floating-Point Arithmetic (May 8, 1978) (Declaration of Joy A. Kruse, Exhibit 8); Jerome T. Coonen, Specifications for a Proposed Standard for Floating Point Arithmetic (June 26, 1978) (Declaration of Joy A. Kruse, Exhibit 9).

[6]Bruce D. Shriver & Peter Kornerup, Paper "The UNRAU: A Unified Representation Arithmetic Unit" Presented to the Computer Arithmetic Symposium at Southern Methodist University (November 19-20, 1975) (Declaration of Joy A. Kruse, Exhibit 26, pp. 5-10).

(1) the scope and content of the prior art; (2) differences between the prior art and the claim(s) at issue; (3) the level of ordinary skill in the pertinent art; and (4) secondary considerations such as commercial success, failure of others, copying, and unexpected results. *Id.* at 17-18, 86 S. Ct. at 694. The key factor at issue here is the difference between the prior art and the claims at issue. Peter Kornerup, a professor at the University of Odense in Odense, Denmark, states that the term "stack of registers," as it is used in the Palmer Patent, was neither "proposed, implemented or suggested" in any product or proposal prior to the filing of the Palmer Patent in 1980. Declaration of Jeffrey R. Chanin, Exhibit 7, para. 6 (Declaration of Peter Kornerup). Since he was the co-author of the UNRAU article, the opinion of Professor Kornerup is particularly persuasive. Moreover, Professor Kornerup's interpretation is supported by Waite. Rebuttal Declaration of Dr. William Waite, paras. 74-76.

Obviousness "'cannot be established by combining the teachings of the prior art to produce the claimed invention, absent some teaching or suggestion supporting the combination.' . . . And, 'teachings of references can be combined *only* if there is some suggestion or incentive to do so.'" *In re Fine*, 837 F.2d 1071, 1075 (Fed. Cir. 1988) (quoting *ACS Hosp. Sys., Inc. v. Montefiore Hosp.*, 732 F.2d 1572, 1577 (Fed. Cir. 1984) (emphasis in original)). Here, Professor Kornerup states that there was "no incentive . . . to adapt or restrict the internal or external data formats of UNRAU to those described in the Coonen article." Declaration of Jeffrey R. Chanin, Exhibit 7, para. 11 (Declaration of Peter Kornerup). Based on the foregoing, the court concludes that Intel has made a clear showing that the Palmer Patent is not invalid due to obviousness.

3. Enforceability

a. *Inequitable Conduct*

ULSI contends that the Palmer Patent is unenforceable because Intel engaged in inequitable conduct during the application for the Palmer Patent and in the reissue proceedings. Specifically, ULSI argues that Intel's patent attorney, Daniel L. Dawes, withheld material prior art and submitted false and misleading declarations and statements to the Patent Office.

A patent may be held unenforceable upon a showing that the applicant engaged in inequitable conduct. When faced with such a contention, the court begins with two questions: first, do "the withheld references satisfy a threshold level of materiality[?]," *Halliburton Co. v. Schlumberger Technology Corp.*, 925 F.2d 1435, 1439 (Fed. Cir. 1991); and second, does "the applicant's conduct satisf[y] a threshold showing of intent to mislead[?]" *Id.* If these two threshold inquiries are satisfied, the court then balances materiality and intent. *Id.*

While ULSI argues that the conduct of Intel before the Patent Office raises a "natural inference" of an intent to deceive, in fact, there is no direct evidence in the record that Intel or Dawes acted with the requisite culpable intent. Dawes apparently considered the prior art at issue to be theoretical and abstract and thus not helpful to him in preparing Intel's application for the Palmer Patent. Intel's Reply Memorandum, p. 29, lns. 1-15. Even if this conclusion could be considered grossly negligent, it would not alone compel a finding of intent to deceive. *Halliburton Co.*, 925 F.2d at 1443. Without something in the record indicating an intent to deceive, the threshold inquiry is not met. The court concludes that Intel has made a clear showing that it did not engage in inequitable conduct before the Patent Office.

b. *License Defense*

ULSI's US83C87 coprocessors are manufactured, in part, by Hewlett-Packard through a foundry services agreement with ULSI. Declaration of Jeffrey R. Chanin, Exhibit 9 (Affidavit of Richard R. Duncombe). Pursuant to this agreement, ULSI provides Hewlett-Packard with a magnetic design tape which contains the physical layout and design for the US83C87 coprocessor. *Id.* at para. 8. After receiving the magnetic design tape, Hewlett-Packard creates a quartz glass plate known as a "reticle" onto which a machine writes a pattern according to the data supplied by the magnetic design tape. *Id.* at para. 9. After creating the reticle, Hewlett-Packard imprints its image on blank silicon wafers. *Id.* at para. 10. As a result, a pattern is created on the wafers which embodies the information provided by the magnetic design tape. *Id.* When this process is complete, Hewlett-Packard inspects and tests the wafers and then ships them to ULSI. *Id.* para. 11.

On January 10, 1983, Intel and Hewlett-Packard entered into a cross-license agreement (the "Intel/Hewlett-Packard agreement"), which provides, in part:

> 1. [HEWLETT-PACKARD] hereby grants INTEL an irrevocable retroactive, nonexclusive, world-wide, royalty-free license under all patents and patent applications owned and controlled by [HEWLETT-PACKARD] having a first effective filing date prior to January 1, 2000, said license to be effective until the expiration of said patents.
>
> 2. INTEL hereby grants [HEWLETT-PACKARD] an irrevocable, retroactive, nonexclusive, world-wide, royalty-free license under all patents and patent applications owned and controlled by INTEL having a first effective filing date prior to January 1, 2000, said license to be effective until the expiration of said patents.

Declaration of Joy A. Kruse, Exhibit 28, p. 2.

On September 17, 1991, the United States Court of Appeals for the Federal Circuit issued an opinion which has prompted the parties to file a total of four additional briefs with regard to the license defense of ULSI. In *Intel Corp. v. United States Int'l Trade Comm'n*, 946 F.2d 821 (Fed. Cir. 1991), Intel sought to prohibit Atmel Corporation (Atmel) (and other parties) from importing into the United States certain Erasable Programmable Read-Only Memories (EPROMs) which allegedly violated one or more of Intel's United States patents. The United States International Trade Commission agreed with a number of Intel's contentions and ordered Atmel to cease and desist its activities with regards to the EPROMs which were found to be infringing. On appeal, Atmel argued, among other things, that its EPROMs were noninfringing because they were manufactured by Sanyo Electric Co. Ltd. and Tokyo Sanyo Electric Co., Ltd. (collectively, Sanyo) under Sanyo's cross-licensing agreement with Intel. The Court of Appeals rejected Atmel's contention, finding its interpretation of the cross-licensing agreement overly broad. *Intel Corp.*, 946 F.2d at 827-28. The court's holding as to this issue is not disputed; however, the parties contest the significance of the following paragraph:

> If the Intel/Sanyo agreement permits Sanyo to act as a foundry for another company for products covered by the Intel patents, the purchaser of those licensed products from Sanyo would be free to use and/or resell the products. Such further use and sale is beyond the reach of the patent statutes. *See United States v. Univis Lens Co.*, 316 U.S. 241, 250-52, [62 S. Ct. 1088, 1093-94, 86 L. Ed. 1408] (1942) (the first vending of any article manufactured under a patent puts the article beyond the reach of the patent).

Intel Corp., 946 F.2d at 826.

ULSI contends that this paragraph "completely disposes of Intel's contentions regarding ULSI's license defense." Defendant's Memorandum of Supplemental Authority, p. 3, lns. 22-23. ULSI contends that Hewlett-Packard acts as a foundry for ULSI, and, therefore, the sale of the wafer for the US83C87 coprocessor is a "first sale" under patent law. Since the US83C87 coprocessor is manufactured under the Intel/Hewlett-Packard agreement, ULSI argues that the US83C87 coprocessor is beyond the reach of the Palmer Patent.

Intel contends that Hewlett-Packard does not sell the wafer for the US83C87 coprocessor to ULSI. Rather, Intel argues that Hewlett-Packard provides a service to ULSI, and because there is no "sale" by Hewlett-Packard to ULSI, there can be no exhaustion of patent rights. Intel further argues that the court's statement in *Intel Corp.* was dicta.

In examining the breadth of the Intel/Hewlett-Packard agreement, it is clear that neither Intel nor Hewlett-Packard intended their agreement to be so broad as to grant the other party the power to sublicense any patent granted under the Intel/Hewlett-Packard agreement. *See* Declaration of Jeffrey R. Chanin, Exhibit 13, para. 5 (Affidavit of Stephen P. Fox). Since both Intel and Hewlett-Packard have attached the same meaning to their contract, the court will interpret the Intel/Hewlett-Packard agreement in accordance with that meaning. *See* Restatement (Second) of Contracts § 201(a) (1979). Accordingly, the court concludes that Intel has shown that the Intel/Hewlett-Packard agreement does not provide ULSI with a license defense to this action.[7]

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[7]Although the court need not reach this issue, the court also finds support for Intel's contention that its patent rights could not be extinguished by Hewlett-Packard's foundry services for ULSI because no *sale* took place. Pursuant to its agreement with ULSI, Hewlett-Packard was to provide foundry *services* for the US83C87 coprocessor. Hewlett-Packard never assumed any ownership rights in any ULSI product and had

4. Conclusion as to Intel's Likelihood of Success on the Merits

As the party seeking injunctive relief, Intel "carries the burden of showing the likelihood of success on the merits with respect to the [Palmer Patent's] validity, enforceability, and infringement." *Nutrition 21 v. United States*, 930 F.2d 867, 869 (Fed. Cir. 1991). While its position could change following a trial on the merits, at this stage of the proceedings, the court finds that Intel has made a clear showing that its patent is valid and that it is being infringed. Further, Intel has also made a clear showing that the Palmer Patent is enforceable. Accordingly, Intel has demonstrated a likelihood of success on the merits.

B. *Irreparable Harm*

A court may presume irreparable harm upon a clear showing of patent validity and infringement. *Smith Int'l, Inc. v. Hughes Tool Co.*, 718 F.2d 1573, 1580-81 (Fed. Cir.), *cert. denied*, 464 U.S. 996, 104 S. Ct. 493, 78 L. Ed. 2d 687 (1983). "This presumption derives in part from the finite term of the patent grant . . . [since t]he opportunity to practice an invention during the notoriously lengthy course of patent litigation may itself tempt infringers." *H.H. Robertson Co. v. United Steel Deck, Inc.*, 820 F.2d 384,390 (Fed. Cir. 1987). Moreover, "[t]he nature of the patent grant . . . weighs against holding that monetary damages will always suffice to make the patentee whole, for the principal value of a patent is its statutory right to exclude."[8] *Id.* The court has

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no right to use or sell any ULSI product. Declaration of Jeffrey R. Chanin, Exhibit 9, para. 13 (Affidavit of Richard R. Duncombe); Declaration of Jeffrey R. Chanin, Exhibit 13, para. 7 (Affidavit of Stephen P. Fox). Therefore, no sale ever took place.

[8]There is, however, no presumption that monetary damages will be inadequate in connection with a motion for a preliminary injunction. *Nutrition 21 v. United States*, 930 F.2d 867, 872 (Fed. Cir. 1991). The

found that Intel has demonstrated a clear showing that the Palmer Patent is valid and infringed. Accordingly, irreparable harm is presumed.

Even if irreparable harm is presumed, this presumption may be overcome by the party opposing the injunction. *Roper Corp. v. Litton Sys., Inc.*, 757 F.2d 1266, 1272 (Fed. Cir. 1985). If the alleged infringer brings forth "clear evidence" showing that the patentee would not actually suffer irreparable injury, the preliminary injunction motion may be denied. *Id.* Although ULSI contends that this presumption is overcome by Intel's delay in seeking the injunction, the court finds no evidence that Intel unreasonably delayed in seeking the injunction.

C. *Balance of Hardship*

Even when irreparable injury is presumed and not rebutted, the court must still consider the balance of hardships. *H.H. Robertson Co.*, 820 F.2d at 390.

> The hardship on a preliminarily enjoined manufacturer who must withdraw its product from the market before trial can be devastating. On the other hand, the hardship on a patentee denied an injunction after showing a strong likelihood of success on validity and infringement consists in a frequently and equally serious delay in the exercise of his limited-in-time property right to exclude. Neither hardship can be controlling in all cases. Because the court must balance the hardships, at least in part in light of its estimate of what is likely to happen at trial, it must consider the movant's showing of likelihood of success. Yet, a court must remain free to deny a preliminary injunction,

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patentee should proffer some evidence, such as the insolvency of the infringer, or the inadequacy of the legal remedy, that money damages will be deficient. *See id.* at 871-72.

> whatever be the showing of likelihood of success, when equity in the light of all the factors so requires.

Illinois Tool Works, Inc. v. Grip-Pak, Inc., 906 F.2d 679, 683 (Fed. Cir. 1990).

Intel contends that the balance of hardships counsels toward granting the injunction. Intel argues that ULSI will not be forced out of business if enjoined from infringing the Palmer Patent; instead, ULSI can perform a minor modification to the US83C87 so that it does not infringe just as other companies have done.

The court does not agree that the balance of hardships favors Intel. Richard Petrarca, Director of Finance for ULSI, states that the US83C87 is ULSI's only product, and, if enjoined from selling the US83C87 coprocessor, ULSI "would in all likelihood be forced out of business." Declaration of Richard W. Petrarca, para. 5.

D. *Public Interest*

The public interest favors the protection of patent rights. However, there is also an interest in a company's right to continue to operate, at least until a claim is resolved by a trial on the merits. Therefore, the court concludes that this factor favors neither party.

CONCLUSION

After weighing the likelihood of success on the merits and the irreparable harm (both of which favor Intel) with the balance of hardships (which favors ULSI), the court concludes that the motion for a preliminary injunction should be granted. The court recognizes the impact an injunction will have on ULSI. This impact, however, is not sufficient to overcome the other factors.

The motion of Intel for a preliminary injunction (#4) is granted.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 92-1116

INTEL CORPORATION,
Plaintiff-Appellee,

v.

ULSI SYSTEM TECHNOLOGY, INC.,
Defendant-Appellant.

ORDER

Aug. 26, 1993.

A combined petition for rehearing and suggestion for rehearing in banc having been filed by the APPELLEE, and a response thereto having been invited by the court and filed by the APPELLANT, and the petition for rehearing having been referred to the panel that heard the appeal, and thereafter the suggestion for rehearing in banc and response having been referred to the circuit judges who are in regular active service,

UPON CONSIDERATION THEREOF, it is

ORDERED that the petition for rehearing be, and the same hereby is, DENIED, and it is further

ORDERED that the suggestion for rehearing in banc be, and the same hereby is, DECLINED.

The mandate of the court will issue on September 2, 1993.

Circuit Judges PLAGER, NEWMAN AND RADER would rehear the appeal in banc.

PLAGER, *Circuit Judge*, with whom NEWMAN and RADER, *Circuit Judges*, join, dissenting from the denial of rehearing *in banc*.

I respectfully dissent from the denial by the full court of Intel's Suggestion for Rehearing *In Banc*. The panel in this case held that a broad cross-license between companies – permitting them to compete rather than litigate – had the effect of immunizing third parties whose products otherwise infringe the patents which were the subject of the cross-license. To reach this result, the panel applied an old rule in a new way, imposing on the cross-license certain contractual effects not provided for in the agreement, not agreed to by the parties to the cross-license (by their own testimony), and directly contrary to the trial judge's findings on the point.

The result frustrates the contracting parties' reasonable commercial expectations, and destroys important property rights they had under the patent laws. No effort was made to justify this result on the grounds of public policy. For the reasons stated in my dissent to the panel opinion, in my view neither precedent nor policy is shown to be furthered by this new rule.

It can be expected that American industry, facing a worldwide competitive environment, will seek new and innovative arrangements for sharing emerging technology. The question raised by the case is whether the law permits American industry to freely share creative assets – patented inventions – by cross-licensing without running the risk of being held to have inadvertently lost the benefits of the patent system. The type of cross-license involved here apparently is not that uncommon, and likely presages a variety of new contractual arrangements among and between industry partners and competitors. Absent a showing of illegality or compelling public policy, it is not the place of courts to limit or expand these arrangements beyond the bounds of the agreements, and in a manner that is avowedly inconsistent

with what the parties intended. Particularly is this so when the consequences of doing so, no matter how well-intentioned, are economically far-reaching and likely to be harmful.

It cannot be denied that *in banc* cases add more to the court's burden. Nevertheless we have demonstrated a willingness to take cases *in banc* to ensure that important principles of law are honored. The rule imposed on this type of cross-license by this case is of sufficient moment to principles of contract law and competitiveness to deserve the attention of, and decision by, the full court. Whether the result is changed or not, I would take the case *in banc* in order to give our decision the benefit of the views of the full court.

Supreme Court, U.S.
FILED
DEC 29 1993
OFFICE OF THE CLERK

No. 93-829

In the Supreme Court of the United States

OCTOBER TERM, 1993

INTEL CORPORATION,
Petitioner,

vs.

ULSI SYSTEM TECHNOLOGY, INC.,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

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BEST AVAILABLE COPY

RULE 29.1 STATEMENT

Respondent ULSI System Technology Inc. has no parent company and no subsidiaries.

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No. 93-829

In the Supreme Court of the United States

OCTOBER TERM, 1993

INTEL CORPORATION,
Petitioner,

VS.

ULSI SYSTEM TECHNOLOGY, INC.,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

INTRODUCTION

Although Intel labors to inflate the significance of this case, nothing in Intel's petition can obscure the highly fact-specific nature, narrow scope, or legal correctness of the decision below. Reduced to its essence, this case is about a drafting choice made by Intel — a multi-billion dollar semiconductor goliath. After entering into a broad patent cross-license with Hewlett Packard ("HP") and reaping the numerous benefits of that agreement, Intel now is displeased with the pro-competitive results of its contract, and it seeks this Court's review to avoid the consequences of its own drafting decision.

The petition offers two arguments for review. First, Intel contends that the opinion below will have broad negative consequences for the semiconductor industry because the decision supposedly permits all cross-licensees to manufacture and sell

products designed by third-party customers. Second, Intel urges that this Court should alter the long-settled patent exhaustion doctrine by holding that a "first sale" requires not only that the seller transfer an article but also that the seller own the intellectual property rights ("design") of the invention embodied in that article. Intel is wrong on both counts.

As written, the Federal Circuit's decision in this case is appropriately narrow and is therefore of limited commercial and legal significance. The opinion below is closely tied to the language of the agreements in this case. Thus, the ruling will have virtually no effect on *future* patent cross-license agreements because — as Intel candidly admits — parties can "contract around this decision," Pet. 17 (emphasis omitted), simply by providing that licensees may sell only products of their own design to third party customers. Nor will the decision significantly impact conduct under *existing* cross-licenses because there is no evidence that the Intel/HP contract at issue here is broadly (or even narrowly) representative of current patent cross-licenses throughout the semiconductor industry. To the contrary, the Federal Circuit's recent decision in *Intel v. ITC*, 946 F.2d 821 (Fed. Cir. 1991), demonstrates clearly that even some of Intel's *own* existing cross-licenses contain provisions specifically anticipating and prohibiting the precise transaction which gave rise to this case. The ruling below therefore is most accurately viewed as enforcing the precise terms of a specific contract that Intel now wishes it had drafted differently. Such a ruling does not warrant a grant of certiorari.[1]

Neither does the Federal Circuit's decision justify modification by this Court of the long-established patent exhaustion doctrine.

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[1] Indeed, the decision below is an exceptionally poor candidate for review because it was issued following a motion for a preliminary injunction, and is not based on a full record developed in a trial on the merits. Moreover, Intel and ULSI have already entered into a settlement concerning the underlying patent infringement allegations in this case. Accordingly, the parties here have very little at stake because a decision by this Court in either party's favor would affect only the amount of the royalty that ULSI already has agreed to pay Intel. *See* Clark, *Intel Loses Ruling on Patents*, S.F. CHRON., June 15, 1993, at C1.

Intel's self-serving theory that a seller must own the "design" of the article sold in order to constitute a "first sale" is wholly unprecedented. The absence of authority for this position is no accident: such a rule would merely exalt form over substance. Intel's theory might, of course, be beneficial to Intel in this one case, but it hardly would prevent the type of transaction about which Intel complains; indeed, under Intel's proposed rule, HP and ULSI could accomplish the very transaction at issue here simply by having ULSI transfer ownership of its "design" to HP in exchange for an exclusive distribution contract.

Intel's proposal, however, is not just easy to circumvent — it is also a bad idea. Requiring that the seller own the "design" of articles sold would frustrate the commercial certainty present under the existing, common sense patent exhaustion rule. Intel's position, if adopted, would open a veritable Pandora's box of new litigation concerning what constitutes a "design" and what it means for a seller to "own" such a design. Accordingly, this Court should decline Intel's invitation to use this easy case to make bad law.

STATEMENT OF THE CASE

This commercial dispute between Intel and ULSI — two semiconductor corporations — concerns the proper interpretation of the specific provisions of two contracts. The first contract is an extremely broad patent cross-license between Intel and HP (another high technology manufacturer), executed in 1983. Under that agreement, HP and Intel granted each other an "irrevocable, retroactive, nonexclusive, worldwide, royalty-free license" for all patents and patent applications filed prior to January 1, 2000. In return for its part in the cross-license, Intel received the dual benefits of access to HP's enormous patent portfolio and reduced exposure to patent litigation.[2]

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[2] These benefits helped fuel Intel's growth from a small concern into the market-dominating giant that it is today. *See Microprocessors: Pent-up demand*, ECONOMIST, Nov. 13, 1993, at 100 (Intel is the world's largest semiconductor corporation).

Six years later, HP entered into the second contract at issue in this case — a foundry agreement with ULSI. This agreement provided that HP would manufacture and then sell to ULSI certain ULSI-designed computer chips. Faced with the resulting new competition, Intel sought to narrow the effective scope of its earlier patent cross-license with HP by bringing this action against ULSI (HP's customer), alleging that the chips manufactured under the HP/ULSI agreement infringed an Intel patent.

The district court, concentrating almost exclusively on technical issues of infringement, mistakenly granted Intel a preliminary injunction. After careful review of the Intel/HP and HP/ULSI contracts, however, the Federal Circuit reversed.

Focusing first on the language of the HP/ULSI contract, the Federal Circuit concluded that the agreement "clearly involved the sale of chips, not merely the sale of fabrication services." 995 F.2d 1566, 1569, 7a. The court rejected Intel's novel argument that HP could not "sell" ULSI the manufactured chips because ULSI had retained intellectual property rights in the "design" of those chips. "Who designed the chip," the court reasoned, has "no bearing on the controlling issue whether [there was a sale]." *Id.* Accordingly, under the terms of the HP/ULSI license, the court found that the chips "were sold by HP to ULSI." *Id.* Noting the well-settled rule of patent exhaustion that "an authorized sale [by a licensee] of a patented product places that product beyond the reach of the patent," *id.* at 1568, 6a (citation omitted), the Federal Circuit concluded that HP's sale of the chips to ULSI "extinguished Intel's patent rights relating to those products." *Id.* at 1569, 7a.

Turning its attention next to the Intel/HP cross license, the court found no provisions in that contract prohibiting the HP/ULSI transaction. Indeed, the court specifically contrasted the Intel/HP agreement with a similar Intel patent cross-license in *Intel v. ITC*, 946 F.2d 821 (Fed. Cir. 1991), which had included an explicit restrictive provision. 995 F.2d at 1570, 9a-10a. Accordingly, the Federal Circuit held that HP was authorized under the Intel/HP agreement to serve as ULSI's foundry. Thus rejecting Intel's infringement claim, the court trenchantly observed that

> [w]hile Intel may not in retrospect be pleased with the deal that it made permitting HP to make unrestricted sales, it nevertheless granted HP that right in 1983, presumably for consideration it believed to be of value at that time. It cannot now renege on that grant to avoid its consequences.

Id. at 1569, 8a.

REASONS FOR DENYING THE WRIT

1. THE FEDERAL CIRCUIT'S DECISION IS FACT-SPECIFIC, AND IS UNLIKELY TO HAVE A SIGNIFICANT IMPACT ON EXISTING OR FUTURE COMMERCIAL RELATIONSHIPS

Despite Intel's protestations to the contrary, the opinion below neither announces a new rule of law nor purports to resolve in general the permissibility of the foundry transaction at issue in this case. Instead, the Federal Circuit's decision simply interprets the particular language of the contracts between Intel, HP, and ULSI, holding — as a matter of contract law — that chips were sold under the HP/ULSI contract and that the Intel/HP cross-license contained no limitations prohibiting the HP/ULSI foundry agreement.

Indeed, the court below could hardly have been clearer in highlighting the fact-specific nature of this case, writing that "if the license had been limited in some relevant way, that would be a *different case* from the one before us." 995 F.2d at 1569, 8a (emphasis added). Thus, the panel found that while Intel might have contractually "retained its right to proceed against those who entered into foundry agreements such as the present one," Intel had in this case failed to do so. *Id.*

At the time of the Intel/HP agreement, Intel was well aware that licensees might serve as foundries for their customers' products. Indeed, Intel itself has "engaged in its own foundry activities with other companies . . . pursuant to which Intel agreed to make and sell integrated circuits wafers or dice that had been designed by those [other] companies." *Cyrix Corp. v. Intel Corp.*, 803 F. Supp. 1200, 1204 (E.D. Tex. 1992), *appeal filed*, No. 93-

1573 (Fed. Cir.) Therefore, Intel's decision to omit any limitations concerning foundry arrangements from the Intel/HP contract was a deliberate choice. Having garnered a decade's worth of benefits under the contract — including access to HP's broad patent portfolio and freedom from litigation with HP — Intel now seeks to rewrite the Intel/HP cross-license.

In order to justify review of the narrow decision below, Intel insists that the Federal Circuit's ruling is of substantial commercial significance. Yet Intel itself concedes that "*future* cross-licenses might explicitly preclude" the HP/ULSI transaction at issue in this case. Pet. 11 (emphasis added). Nevertheless, in a whirlwind of hyperbole, Intel contends that the Federal Circuit's ruling will have dire consequences not only for the entire semiconductor industry but also for the American economy at large.[3]

The unspoken premise of Intel's argument, of course, is that all (or at least most) *existing* patent cross-license contracts — both inside and outside the semiconductor industry — are identical to the HP/Intel agreement in this case. This premise remains unspoken, however, because Intel has not presented a scintilla of evidence that the precise terms of the Intel/HP contract are common to many, or any, other existing patent cross-licenses.

To the contrary, the information available demonstrates that even Intel's own patent cross-licenses often differ from the Intel/HP agreement here, and that straightforward differences in contractual language may result in different outcomes. In *Intel v. ITC*, 946 F.2d 821 (Fed. Cir. 1991) [hereinafter "*Atmel*"], the Federal Circuit specifically addressed the question presented in this case. The *Atmel* court, however, reached the opposite result solely because the Intel cross-license there at issue contained a

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[3] Intel also asserts, without citation to *any* authority, that the opinion below will "exacerbate the trend to send manufacturing jobs overseas." Pet. 16. Because the Federal Circuit's decision is quite narrow, it likely will have little effect in either direction on the domestic job market. Nevertheless, the only facts available concerning the impact of the ruling below — namely, the facts of this case — suggest just the *opposite* of Intel's argument: the HP/ULSI foundry agreement provided manufacturing work for HP's American employees.

simple limitation not included by the parties in the Intel/HP cross-license in this case.

The parallels between *Atmel* and this case are striking. As here, Intel had entered into a "world-wide, royalty-free" patent cross-license with another chipmaker (Sanyo). *Id.* at 828. As here, a third party customer (Atmel) designed a computer chip and engaged the Intel cross-licensee (Sanyo) to manufacture the chip. And as here, Intel then sued the customer, alleging patent infringement, and the customer responded by arguing that it was immune from infringement liability because it had purchased the allegedly infringing chips from an Intel licensee.

In *Atmel,* however, the Federal Circuit ruled in Intel's favor, holding that the customer was *not* immune from infringement liability because the Intel/Sanyo contract only permitted Sanyo to include and sell Intel's patented inventions in "any Sanyo . . . product." *Id.* at 826 (internal quotation marks omitted). This single, straightforward contractual limitation made all the difference, and the license was "properly construed to cover only Sanyo designed and manufactured products and to exclude parts designed by others." *Id.* at 828. Thus, the *Atmel* court, as a matter of contract interpretation, concluded that the cross-license in that case "preclude[d] the . . . foundry manufacture by Sanyo of [a customer-designed chip]." *Id.*

In contrast, "the licensing agreement between Intel and HP here contains no restriction on HP's right to sell or serve as a foundry." 995 F.2d at 1570, 10a. Accordingly, the Federal Circuit in this case read the Intel/HP cross-license to permit HP's manufacture and sale of products designed by ULSI. Taken together then, the Federal Circuit's decisions in *Atmel* and this case illustrate that the appropriateness of a particular foundry arrangement, such as the HP/USLI agreement, is a fact-specific matter depending on the precise wording of a given patent cross-license. Thus, the narrow decision below is manifestly inappropriate for this Court's review.

2. THE FEDERAL CIRCUIT'S DECISION IS FULLY CONSISTENT WITH THIS COURT'S LONG-SETTLED PATENT EXHAUSTION DOCTRINE

For well over a century, it has been settled law that when a patentee "sells a [patented] machine or instrument" for consideration, that machine or instrument "passes without the limit of the monopoly." *Adams v. Burke,* 84 U.S. 453, 456 (1873). This patent exhaustion doctrine exists "to give effect to the public policy which limits the granted monopoly strictly to the terms of the statutory grant." *United States v. Univis Lens Co.,* 316 U.S. 241, 250 (1942). Indeed, this Court's decisions uniformly have recognized that

> the purpose of the patent law is fulfilled with respect to any particular article when the patentee has received his reward for the use of his invention by the sale of the article, and that once that purpose is realized the patent law affords no basis for restraining the use and enjoyment of the thing sold.

Id.

This same longstanding patent exhaustion doctrine applies to the authorized sale of a patented article by a licensee. 995 F.2d at 1568, 6a; *see also Unidisco, Inc. v. Schattner,* 824 F.2d 965, 968 (Fed. Cir. 1987), *cert. denied*, 484 U.S. 1042 (1988). Thus, the court below found that, by signing the Intel/HP cross-license and thereby receiving the many benefits of that agreement, Intel had received its just reward for the invention at issue in this case. The Federal Circuit then closely examined the terms of the HP/ULSI contract and determined as a matter of contract law that "the agreement clearly involved sale of chips" embodying Intel's patented invention. 995 F.2d at 1569, 7a. Accordingly, the sale of those chips "by HP to ULSI . . . extinguished Intel's patent rights relating to those products." *Id.*

In seeking review of this straightforward decision, Intel now proposes that this Court effect a dramatic modification of the time-honored patent exhaustion doctrine. Intel argues that the sale of a patented article should not be deemed to exhaust the patentee's monopoly unless the seller (patentee or licensee) owned not only the patented article itself but also the "design" of

that article. Such a rule, however, would be unprecedented, unwarranted, and unwise.[4]

1. There simply is no authority holding that a seller must own intellectual property rights to the "design" embodied in an article in order to make a patent-exhausting sale of that article. To the contrary, this Court clearly has stated that all that is necessary to invoke the patent exhaustion doctrine is "the sale of an *article* embodying the invention." *Univis Lens*, 316 U.S. at 250 (emphasis added). When a licensee makes an authorized sale, that sale "exhausts the monopoly *in that article* and the patentee may not

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[4] Intel also contends that its patent monopoly was not exhausted by the HP/ULSI transaction because HP did not "own" the computer chips it transferred to ULSI, or alternatively, because HP sold only manufacturing "services" under the HP/ULSI contract. Pet. 24-25. These arguments, however, are directed solely at the Federal Circuit's interpretation of the particular language of the HP/ULSI contract. That interpretation clearly was correct given that the HP/ULSI contract "recite[d] prices for the chips and include[d] a delivery schedule for shipments of the chips to ULSI" and was "replete with references to the sale of semiconductor wafers." 995 F.2d at 1569, 7a (emphasis added). Moreover, Intel simply is wrong in suggesting that HP did not "own" the chips: if ULSI had refused to pay HP the agreed-upon price for those products, HP would have been entitled to (and would have) kept the chips for itself. *See* C.A. App. A49 ("Should Buyer become delinquent in the payment of any sum due hereunder, HP shall not be obligated to continue performance.") Whether or not HP would then have been free to sell those chips to another buyer is irrelevant. *See Unidisco*, 824 F.2d at 968 (transfer of ownership constitutes patent-exhausting sale despite seller's agreement to sell exclusively to single buyer). HP owned the chips until ULSI paid for them, and HP's transfer of those chips to ULSI in return for monetary remuneration therefore constituted a sale. In any event, Intel's arguments about "ownership" and "services" are matters concerning the interpretation of a single contract, are wholly independent of the proper construction of the patent exhaustion doctrine, and therefore do not warrant review by this Court.

thereafter, by virtue of his patent, control the use or disposition *of the article." Id.* (emphasis added).[5]

Thus, Intel's argument reduces to a request that this Court reconsider the time-honored patent exhaustion rule most recently reaffirmed in *Univis Lens*, solely for the purpose of expanding the ambit of Intel's monopoly. But this Court "[does] not [lightly] expand patent rights by overruling or modifying [its] prior cases." *Deepsouth Packing Co. v. Laitram Corp.*, 406 U.S. 518, 531 (1972). Instead, this Court consistently has required

> a clear and certain signal from Congress before approving the position of a litigant who . . . argues that the beachhead of privilege is wider, and the area of public use narrower, than courts had previously thought.

Id. As in *Deepsouth*, "[n]o such signal legitimizes [Intel's] position in this litigation." *Id.*

Moreover, there is nothing about the factual circumstances of this case requiring a revision of this Court's long-settled rule. In fact, the "Federal Circuit has consistently applied the Patent Exhaustion Doctrine in a variety of contexts, including situations involving foundry relationships in which a foundry manufactures products to a customer's design." *Cyrix*, 803 F. Supp. at 1213. In *Atmel*, for example, the Federal Circuit considered a foundry relationship similar to the HP/ULSI contract in this case and held that where an agreement

> permits [a licensee] to act as a foundry for another company for products covered by the Intel patents, the purchaser of those licensed products from [the licensee] would be free to use and/or resell the products.

946 F.2d at 826.[6]

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[5] "Intel does not dispute that HP was authorized under the broad terms of the [Intel/HP] licensing agreement to sell the chips at issue." 995 F.2d at 1569, 7a.

[6] *See also Cyrix*, 803 F. Supp. at 1214 ("An authorized sale of a patented product exhausts the patent monopoly as to that product.")

Indeed, "a conventional sale is not required to trigger patent exhaustion." *Id. Any* transfer of ownership places the article transferred beyond

Accordingly, the Federal Circuit ruled that Intel's argument "confuses the issue of design origin with the issue of sale." 995 F.2d at 1569, 7a. Whether HP or ULSI owned the "design" etched into the computer chips at issue has "no bearing on the controlling issue whether the [chips] were sold by HP to ULSI and thus extinguished Intel's patent rights relating to those products." *Id.*

2. Not only is Intel's theory unprecedented, it also is an impermissible and ineffectual attempt to regulate form rather than substance. Adoption of Intel's view that a seller must own both the article and the "design" embodied in that article in order to make a patent-exhausting sale would not prohibit transactions identical in substance to the sale at issue in this case. Instead, under Intel's alternative formulation of the patent exhaustion doctrine, form would be outcome-determinative. Parties wishing to replicate the HP/ULSI transaction could simply contract for the customer (ULSI) to transfer ownership of its "design" to the licensed foundry (HP) in return for an exclusive distribution contract. Alternatively, the customer could license its "design" to the foundry for the purpose of manufacturing the desired article.[7] In either event, the foundry would own rights to the "design" and

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the reach of the patent statute. *See id.; Harshberger v. Tarrson,* 87 F. Supp. 43, 45-46 (N.D. Ill. 1949), *aff'd,* 184 F.2d F.2d 628 (7th Cir. 1950) (patentee's monopoly ended once an article embodying the patented invention was made and "disposed of" to a third party, even though the article was transferred as a result of a security pledge rather than by a sale.)

[7] The mere act of transferring a "design", whether or not for consideration, would not in itself constitute patent infringement. *See* 35 U.S.C. § 271(a); *Deepsouth,* 406 U.S. at 528 ("[P]atent protects only against the operable assembly of the whole"); *see also Paper Converting Mach. Co. v. Magna-Graphics Corp.,* 745 F.2d 11, 16 (Fed. Cir. 1984) (Patentee may "prevent anyone from making, selling, or using a structure embodying the invention, but the monopoly goes no further than that.") Thus, because ULSI could have transferred ownership of or licensed its "design" (a magnetic tape) to HP without "making, using, or selling" any portion of the patented invention (a computer chip), ULSI could have completed such a transfer or license without infringing Intel's patent.

could — by Intel's own reasoning — sell articles embodying that design to the customer free of the patentee's monopoly.

Intel's theory thus is the ultimate elevation of form over substance, and "[t]his Court has quite consistently refused to allow the form into which the parties chose to cast the transaction to govern." *United States v. Masonite Corp.*, 316 U.S. 265, 276 (1942). Moreover, because parties could easily circumvent Intel's rule, that rule would do little more than resolve this single case.

3. Finally, adoption of Intel's novel theory would complicate enormously the heretofore straightforward patent exhaustion doctrine. Under existing, well-settled law, a court need only determine whether an authorized licensee sold a customer an article embodying a patented invention. Intel's theory, however, would require the courts to define the "design" of each article and then to determine who "owns" that design. Such a regime would raise a plethora of new questions. What is the "design" of a complex product consisting of multiple intellectual property components? Who owns the design if the customer and the patent licensee create the design as a joint venture? Who owns the design if the customer licenses its own design to the patent licensee? If the customer pays the patent licensee to develop a design, would the patent licensee then own the design? If so, why should the result be different if the customer simply pays its own employees to develop the design in the first instance? All of these unresolved questions would undermine existing certainty and would frustrate parties' ability to contract effectively. *Cf. Planned Parenthood v. Casey*, 112 S. Ct. 2791, 2803 (1992) ("Liberty finds no refuge in a jurisprudence of doubt.")

* * *

In summary, Intel's petition seeks certiorari in order to escape the consequences of its own decision to enter into a broad, unrestricted patent cross-license. Having handsomely benefitted from that cross-license, Intel now attempts to avoid fulfilling its part of the bargain. The Federal Circuit — viewing this matter as a case of contract interpretation — properly rejected this attempt by Intel to modify its own contractual obligations. The court recognized the fact-specific nature of this case and refused to

endorse Intel's entirely unprecedented reformulation of settled patent exhaustion doctrine. The Federal Circuit was correct, and its opinion therefore presents no occasion meriting this Court's review.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

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In the Supreme Court of the United States

OCTOBER TERM, 1993

INTEL CORPORATION, PETITIONER

v.

ULSI SYSTEM TECHNOLOGY, INC., RESPONDENT

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

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REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONER

The Federal Circuit's sharply divided ruling in this case has been widely publicized as a ground-breaking decision with far-reaching implications. We showed in the petition that the decision fundamentally misconceived an important issue of patent law. We also explained the substantial economic effects that follow from the lower court's distortion of the patent exhaustion doctrine, opening up a broad range of licensed patents to exploitation by opportunistic imitators. Ignoring the two dissenting opinions below, all of the commentary on this case, and all of our arguments on the merits, however, ULSI's brief in opposition insists that this is a routine case heavily dependent on idiosyncratic facts.

ULSI cannot avoid the obvious simply by clenching its eyes shut. Judges and commentators agree that the case has broad implications as a matter of patent law, for, as ULSI itself once admitted, this case turns on the law of patents, not contracts. It is beyond serious dispute that the outcome of this case, no matter who wins, will have a significant impact on how business is conducted in at least the semiconductor industry. The lower court's new twist on patent exhaustion rests on neither reason nor precedent, while the proper resolution of the issue will restore economic sense to this part of our intellectual property regime. The decision fully merits review by this Court.[1]

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[1] ULSI suggests in passing that the posture of this case (a reversal of a preliminary injunction) might make it inappropriate for review by this Court. Br. in Opp. 2 n.1. The Federal Circuit made clear, however, that it was ruling dispositively on questions of law. See Pet. App. 9a, 10a; see also Pet. 8 & n.3. ULSI also notes that the parties have entered into a conditional settlement that provides for royalty payments regardless of the outcome of this litigation but provides for a larger royalty if the preliminary injunction stands. This Court has repeatedly held that such conditional settlements do not undermine the necessity for or appropriateness of resolution by this Court of important issues of law. *Nixon* v. *Fitzgerald*, 457 U.S. 731, 743-744 (1982); *Havens Realty Corp.* v. *Coleman*, 455 U.S. 363, 370-371 (1982). If the Court is ever going to review the question presented by the petition, it is appropriate to do so in *this* case, and not to await some possible future case in which a party might have the fortitude to preserve this issue in litigation up through the Federal Circuit notwithstanding the definitive *ULSI* precedent.

1. To read the brief in opposition, one would think that this is an "easy case" (Br. in Opp. 3) in which the Federal Circuit, without dissent, corrected a painfully obvious error by the district court. In fact, a detailed panel dissent was followed by three judges' dissent from the denial of rehearing en banc, and both opinions persuasively explained that the sweeping rule of law announced by the panel majority is legally incorrect and practically important. Pet. App. 11a-23a, 40a-42a. The two district courts to consider the issue reached diametrically opposed conclusions. And the only circuit court to address the same issue before the creation of the Federal Circuit dismissed out of hand the rationale adopted in this case. See Pet. 2.

ULSI also pretends before this Court that the importance of this case is limited to "the precise wording of a given patent cross-license." Br. in Opp. 7. When the court of appeals issued its decision, ULSI's own spokesman was far more candid, announcing that the decision had "ramifications * * * for the entire semiconductor industry." *Intel, Clone Maker ULSI at Odds Over Federal Court Decision*, PC WK., July 5, 1993, at 106. Commentators from the intellectual property bar agreed that the Federal Circuit's "treatment of the doctrine of patent exhaustion has far reaching implications for a broad range of technologies." Martin, Intel Corp. v. ULSI System Technology, Inc.: *Patent Exhaustion and Post-Sale Restrictions on the Use of a Component Made Under License*, 2 TEX. INTELL. PROP. L.J. 5, 6 (1993). See also, *e.g.*, Hustein & Greguras, *Impact of the ULSI Case on High-Technology Industry*, S.F. DAILY J., Nov. 9, 1993, at 5 ("It cannot be over-emphasized that the ULSI case is not limited to semiconductors."); Hustein & Greguras, *Cross-License Agreements Can Circumvent Patent Infringement*, S.F. DAILY J., Nov. 8, 1993, at 5; Abramson, *When the Chickens Come Home to Roost: The Licensed Foundry Defense in Patent Cases*, COMPUTER LAW., Mar. 1993, at 1, 1 (noting "intense interest" and "considerable controversy" surrounding district court decisions).

2. Contrary to ULSI's assertions, the Federal Circuit's decision does not turn on the presence of "precise terms" (Br. in

Opp. 6) in the patent license agreement.[2] It rests on the *absence* of language that *prevents* the licensee from performing fabrication services for third parties. Pet. App. 7a-10a. The patent license agreement is relevant only to the extent that it imposes "no restriction on HP's right to sell or serve as a foundry" (Pet. App. 10a), but that "right to sell" matters only if the ULSI/HP transaction is a "first sale." All licensed patents are open to predation unless the terms of the license reflect that the patentee clearly "retained its right to proceed against those who entered into foundry agreements such as the present one." Pet. App. 8a.[3] Those are rules of patent law determining the rights of the patent holder vis-à-vis the imitator; like all rules determining the relative rights of private parties, they can be altered by contract, but that fact hardly makes them into mere rules of contract law. See also Pet. 23 n.10; *Keeler* v. *Standard Folding Bed Co.*, 157 U.S. 659, 666 (1895).

ULSI's attempt to repackage the issues in this case as matters of contract is of strikingly recent vintage. ULSI successfully

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[2] ULSI mischaracterizes this patent dispute between Intel and ULSI as a contractual dispute between HP and Intel. Br. in Opp. 4 ("Intel sought to narrow the effective scope of its earlier patent cross-license with HP by bringing this action"). Intel has no quarrel with HP, does not object in the least to HP's performance of foundry services, and has no desire to alter its agreement with HP. Intel asserts only that the performance of foundry services by HP for an infringer of an Intel patent does not have the *legal effect* of relieving the infringer – ULSI – of responsibility for its imitative activity. Of course, ULSI, like every infringer, asserts that it is "pro-competitive" to ignore Intel's patent. Br. in Opp. 1. But the patent laws *do* stifle competition – competition from those who choose to imitate rather than innovate – in order to provide a proper incentive for inventors.

[3] Contrary to ULSI's perception of the HP license as somehow unique, it is typical for patent licenses *not* to include an anticipatory repudiation of the rule announced below. For example, in the pending case of *Cyrix Corp.* v. *Intel Corp.* v. *Texas Instruments, Inc.*, No. 4:92cv52 (E.D. Tex.), Intel's cross-licenses with Texas Instruments and SGS-Thomson are alleged to give rise to the "licensed foundry" defense announced in *ULSI*.

insisted below that "sale by a licensed foundry, unless otherwise restricted in the license, is a 'first sale.'" C.A. Reply Br. 9. ULSI argued that, unless that broad premise of patent law were valid, "there would have been no reason" for the court of appeals in *Intel Corp.* v. *ITC*, 946 F.2d 821 (Fed. Cir. 1991) (*Atmel*), "to address the more difficult and fact-specific inquiry" into the meaning of the patent license agreement. *Ibid.*

Only because of its important (and erroneous) holding of patent law did the Federal Circuit majority devote any of its attention to interpreting a contract, and the contract it interpreted was not the Intel/HP license agreement.[4] The majority thought that this case "turns on whether there was a sale of 'C87 coprocessors by HP to ULSI" (Pet. App. 6a) and sought to resolve that issue by interpreting the *ULSI/HP foundry services agreement*. Whether there was a "sale" of the sort that allows ULSI to "resell" with impunity otherwise-infringing products, however, should turn on the rationale and scope of the first-sale doctrine of patent law, not on the terms of a contract to which the patent holder is not a party. The majority's error was not misinterpreting a contract, but misinterpreting patent law. See Pet. App. 15a (panel dissent).

Ironically, ULSI tries to hide behind the characterization of the transaction as a "sale" in the ULSI/HP agreement at the same time that it quotes (Br. in Opp. 12) the observation in *United States* v. *Masonite Corp.*, 316 U.S. 265, 278 (1942), that "this Court has quite consistently refused to allow the form into which the parties chose to cast the transaction to govern." As we

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[4] The panel dissent observed that the evidence indicated "unequivocally" that neither HP nor Intel intended their agreement to shield third parties like ULSI (Pet. App. 19a), and the majority did not dispute the dissent on that point, which of course would be critical if this case turned on interpretation of the Intel/HP contract. Rather than treating this as a case in which the intent of the parties to *that* contract mattered, however, the majority insisted that the *only* thing that mattered was whether HP "sold" the chips to ULSI. Pet. App. 6a-8a. Thus, to determine the rights of *Intel*, the majority looked to the intent of *HP and ULSI* in framing *their* contract, not the Intel/HP contract as ULSI contends.

explained in the petition (at 19-20), the *substance* of the ULSI/HP transaction is that of author (ULSI) and custom printer (HP). If the author's work illicitly copies another, it is absurd to contend that the printer's license to print the other work somehow protects the author as well. The printer does not sell the author his work, though the printer does demand payment for the printed volumes.

To reach the contrary conclusion, the Federal Circuit merely seized on the caption of the ULSI/HP contract to determine that in some sense the agreement was a "sale." Pet. App. 7a. In the lower court's view, if HP sold ULSI anything, the transaction must exhaust Intel's patent. That conclusion is insupportable. The patent laws do not protect factory labor or raw materials, but rather the invention – the intellectual property – embodied in an article. A "sale" cannot dissipate patent rights unless the invention subject to the patent has been sold. As we demonstrated (Pet. 23-25), HP did not sell the invention embodied in ULSI's chips to ULSI, any more than would a delivery driver who dropped the chips at ULSI's loading dock C.O.D. HP did not own ULSI's infringing invention; it could not copy ULSI's infringing invention; it could not sell ULSI's infringing invention; and it did not legitimate ULSI's infringing invention. ULSI provides no coherent response to these points.

3. From ULSI's pious pronouncement about "overruling or modifying * * * prior cases," one would think that Intel had explicitly asked this Court to overrule *United States* v. *Univis Lens Co.*, 316 U.S. 241 (1942). See Br. in Opp. 10. In fact, Intel pointed out (Pet. 25-28) the compelling reasons why *Univis Lens* does not support (but actually undercuts) the decision below.[5] ULSI completely ignores those reasons.

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[5] ULSI cites (Br. in Opp. 10) *Deepsouth Packing Co.* v. *Laitram Corp.*, 406 U.S. 518 (1972) (rejecting extraterritorial application of 35 U.S.C. § 271(a)), but it is unclear how *Deepsouth* pertains to this case, except that the decision below, more than *Deepsouth*, promises "unduly to reward the artful competitor who uses another's invention * * * and who seeks to profit thereby." *Id.* at 532-533 (Blackmun, J., dissenting).

This Court said in *Univis Lens* that the kind of sale necessary to "exhaust" a patent is "the vehicle for transferring to the buyer ownership of the invention with respect to that article" (316 U.S. at 252) and that patent exhaustion occurs only when there has been "a complete transfer of ownership" of an article that is "within the protection of the patent law" (*id.* at 249). Both statements clearly distinguish *Univis Lens* from this case, but ULSI ignores these important limitations on the holding of *Univis Lens* and treats ownership as irrelevant. Br. in Opp. 8-9 & n.4.[6] Under a proper reading of *Univis Lens*, however, ownership is critical: HP could not sell what it did not own. See Pet. 25.

Although there was a physical transfer of a product in this case, the resemblance to *Univis Lens* stops there. In *Univis Lens*, the "buyer" did not already own the design of the article sold, and the reasoning in that case makes quite clear that the ownership of the *invention* lies at core of the patent exhaustion doctrine. No invention changed hands in this case. Far from asking this

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[6] Understandably lacking the courage of its convictions, ULSI also asserts that HP *did* own the math coprocessors and therefore *did* transfer ownership when it "sold" them to ULSI. Br. in Opp. 9 n.4 ("Intel simply is wrong in suggesting that HP did not 'own' the [ULSI] chips"). But that assertion appears for the very first time in this Court. ULSI made no effort in the district court to dispute an HP representative's sworn testimony that "HP has no ownership rights to ULSI's products." C.A. App. A413. Relying on that affidavit, the district court observed that HP "never assumed any ownership rights in any ULSI product and had no right to use or sell any ULSI product." Pet. App. 36a n.7. ULSI did not challenge that observation on appeal, the panel majority did not take issue with it, and the panel dissent specifically agreed with it (Pet. App. 21a-22a). In any event, ULSI's new-found claim that HP owned ULSI's chips is preposterous. See Pet. 24-25. ULSI's definition of ownership apparently does not include one of the most important sticks in the bundle of property rights: the right to convey the property to others. Br. in Opp. 9 n.4 ("Whether or not HP would then have been free to sell those chips to another buyer is irrelevant."). Like a lawyer's "retaining lien" or ability to retain his client's papers and other property until he receives his fee (see 7A C.J.S. *Attorney & Client* § 358 (1980)), HP's ability to keep the math coprocessors if ULSI did not pay for them reflected a security interest, not ownership.

Court to overrule *Univis Lens*, we ask the Court for a thoughtful application of that case – and other cases applying the first-sale doctrine in a patent infringement context rather than the antitrust context of *Univis Lens* – to an emerging and controversial tactic for dodging patent infringement claims.

4. ULSI also pretends to believe that Intel's theory is "unprecedented" and that the applicability of the first-sale doctrine to the facts of this case is so clear that no one could possibly question it. In fact, application of the first-sale doctrine to facts like these was rejected long ago in *Timken* v. *Olin*, 41 F. 169, 171 (C.C.S.D. Ohio 1890), was rejected by the district court in this case (Pet. App. 34a-36a), and is so controversial that the issue has prompted not only sharp differences of judicial opinion but also a spate of articles, both before and after the decision below, all trumpeting the profound implications of that novel decision. See articles cited at p. 2, *supra*. See also Orenstein, *Chip Makers Given New Defense Against Infringement Claims*, THE RECORDER (S.F.), June 15, 1993, at 1.

ULSI decries the supposed threat to "commercial certainty" (Br. in Opp. 3) posed by a rational interpretation of the first-sale doctrine in the foundry context. As the three judges dissenting from denial of rehearing en banc pointed out, it is the decision below that "frustrates * * * reasonable commercial expectations, and destroys important property rights * * * under the patent laws" as well. Pet. App. 41a. ULSI ignores the fact that for one hundred years the *only* authority on a foundry arrangement of this kind had summarily rejected ULSI's position. *Timken* v. *Olin*, *supra*. In the intervening century, it seems, no one was bold enough to advance the argument embraced by the current crop of computer chip imitators. To the extent that there was commercial certainty, it was the certainty that one could not launder one's infringing product by hiring a licensee to manufacture it.[7]

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[7] As a corollary to its pretense that Intel's position would overturn "well-settled" law, ULSI attempts through a series of hypothetical questions to show that Intel's position "would complicate enormously the heretofore straightforward patent exhaustion doctrine." Br. in Opp. 12. Whatever complexities may inhere in complex hypothetical situations,

In fact, the decision below is the first appellate case *ever* to excuse patent infringement by applying the first-sale doctrine to a patent laundering arrangement. Not until the Federal Circuit included certain dicta in its *Atmel* decision (ruling in favor of the patentee) in 1991 had any court even hinted that the patent exhaustion doctrine might be a device for opportunistic imitators to avoid paying for the use of a patent; not until the district court decision in *Cyrix Corp.* v. *Intel Corp.*, 803 F. Supp. 1200 (E.D. Tex. 1992), appeal pending, No. 93-1573 (Fed. Cir.), did any court hold that a laundering arrangement actually exhausted a patent. The supposed "certainty" that ULSI asks this Court to respect dates at the earliest from June 1993, when the panel decision below resolved the conflict between recent district court opinions.

Still more tellingly, neither ULSI nor the Federal Circuit identified *a single case* in which a so-called "sale" was held to have exhausted patent rights even though the purchaser had supplied the design function, the invention, the intellectual property. ULSI's adamant insistence that the ownership of the design was not determinative in this Court's prior cases is wholly irrelevant because the issue simply was not presented. In *none* of those cases was the design function performed by anyone other than the patentee or licensee, and there was no reason for the courts to anticipate such an arrangement. The first-sale doctrine has *always* been applied to protect innocent purchasers who had nothing to do with the intellectual property involved, except that they wanted to use or to sell a patented article that they had bought. Not until this case (and the district court decision in *Cyrix*) has the first-sale doctrine been misapplied to protect unlicensed commercial imitators of patented products.

5. ULSI ironically complains that to apply the first-sale doctrine to foundry agreements as we propose would "regulate form

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however, there is nothing particularly intricate about this case. ULSI designed a math coprocessor that infringes an Intel patent, and it sought to evade the patent law by having an Intel licensee, HP, manufacture its infringing product. A desire to avoid complexity is no justification for blessing that blatant scheme.

rather than substance." Br. in Opp. 11. As we explained in the petition (at 19-25), the decision below truly ignored substance in favor of form: the court of appeals relied on the fact that the "Agreement [for] fabrication of an integrated circuit designed by ULSI" (C.A. App. A38) was *captioned* a "sale." Pet. App. 7a.

ULSI also suggests that parties could "circumvent" a decision in Intel's favor. Br. in Opp. 11-12. It is scarcely news that parties will adjust to whatever rule of law governs an economic relationship. See generally Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

But ULSI is quite wrong to suggest that a transfer of the design to the patent licensee produces a transaction that is "identical in substance to the sale at issue in this case." Br. in Opp. 11.[8] On the contrary, in both economic and legal significance that transaction is substantially *different* from the transaction in this case. Most critically, the licensee (HP) would own the invention that it fabricated and sold to the purchaser. The imitating designer then would have to bargain for – and pay for – the privilege of using the licensed patent rights. It would be quite clear that the imitator sought the licensee's ability to provide protection from infringement lawsuits, protection for which the imitator likely would have to pay dearly if it wanted to use a valuable patent. In this case, by contrast, it is clear that ULSI successfully hid from HP its intention to benefit from HP's patent rights. See Pet. 7; C.A. App. A411. Moreover, there would be an important legal consequence if HP became the owner of ULSI's design: any intellectual property rights inhering in that design would automatically be shared with Intel under the Intel/HP patent license. Under the existing arrangement and the

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[8] ULSI's other example (Br. in Opp. 11) – "licens[ing] its 'design' to the [licensed] foundry [HP] for the [exclusive] purpose of manufacturing the desired article" – would *not* amount to a transfer in ownership of the design and would *not* exhaust Intel's patent rights for the reasons amply explained in the petition (at 19-29).

Federal Circuit's holding, by contrast, ULSI gets the benefit of Intel's patent while sharing *nothing* with Intel.[9]

Much as ULSI would like this Court to believe otherwise, this case is not *Univis Lens*; the sharply divided opinions below do not reflect the routine application of established law; and this highly publicized case does not present a narrow, fact-dependent issue. This case presents a novel issue of substantial importance, and the decision below rewards imitators and punishes America's innovators for no sufficient reason.

For the foregoing reasons and those given in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted.

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[9] ULSI asserts that Intel has received its "just reward" from the HP/Intel agreement, and that therefore ULSI should have the same design freedom for which HP bargained and paid. Br. in Opp. 8. Yet ULSI has paid no price to anyone for the use of Intel's patent. See Hustein & Greguras, *supra*, S.F. DAILY J., Nov. 9, 1993, at 5. Surely Intel received no reward whatsoever for ULSI's infringing coprocessor.